**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

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

REPLY BRIEF OF THE OFFICE OF THE PUBLIC COUNSEL

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COMES NOW the Office of the Public Counsel ("OPC" or "Public Counsel") and for its Reply Brief states as follows:[1]

Noranda AAO

The Commission's determination to "grant" Ameren Missouri an Accounting Authority Order ("AAO") for the "unrecovered fixed costs" or "lost/ungenerated revenue" arising out of the 2009 Ice Storm was, contrary to Ameren Missouri's assertions, a rather limited action. In granting the AAO to Ameren Missouri, the Commission made no rate-making determination at all. Indeed, the Commission said as much in its order. Report and Order, Case No. EU-2012-0027, p. 4 (Nov. 26, 2013) (Doc. No. 164). And the language in that order was such that **____

____ ** (Ex. 244 HC). As a result,**____

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______________________**

Rather, what the Commission did in the AAO proceeding was engage in the narrow act of permitting Ameren Missouri to make an accounting entry in a special regulatory account so that

[1] Any issue or argument treated in Public Counsel's Post-Hearing Brief not addressed specifically below is hereby adopted and incorporated as if set forth fully herein.

the sum could be considered at a later rate case for potential inclusion in rates. Without the Commission's prior action, the current discussion of including the AAO in rates would be foreclosed. And so, in effect, the Commission's prior decision was a vote merely to keep the AAO issue alive until this rate case; it was not and should not be considered dispositive of the AAO's treatment now. Ameren should not be permitted in the deferral case to use the argument that "this is not ratemaking" as a sword in favor of granting the AAO and then in the rate case argue "but the Commission has already granted it" as a shield against disallowing any consideration of the proper ratemaking treatment it should receive.

To be clear, the AAO authorized by the Commission for the Noranda ice storm, even if a permissible deferral, cannot be recovered in rates. Ameren Missouri's brief does an admirable job of blurring the line between AAO deferrals and recoveries (Ameren Br. at 29-31). Ameren would have this Commission believe that when an AAO deferral has been granted, successful recovery is mandated in every instance save for imprudence or mathematical miscalculation (Ameren Br. at 30). This is simply not the case. The legal standard governing whether an amount may be recovered in rates is set by statute as interpreted in *State* ex rel. *Utility Consumers' Council of Mo., Inc. v. Pub. Serv. Comm'n*, 585 S.W.2d 41 (Mo. 1979) ("*UCCM*").

Ameren Missouri asserts this AAO is intended to permit it to recoup revenue that went un-generated in a prior period which putatively left certain fixed costs associated with Noranda's class unrecovered (Ameren Br. at 23-24). As the Missouri Supreme Court stated in *UCCM*, "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…they **cannot be used to set future rates to recover for past losses** due to imperfect matching of rates with expenses." *UCCM, 585 S.W.2d at 58* (emphasis added). While it may, or may not, have been lawful for the Commission

to authorize an accounting entry for the AAO as requested by Ameren Missouri in the deferral proceeding, to recover that amount in rates is clearly prohibited.

If an AAO is ever lawful, which OPC does not concede, it is only lawful in those instances in which extraordinary past expenses are being considered as a basis for what is reasonable to charge going forward in order to avoid further future losses.[2] Ameren's argument for recovery of the AAO, that it reflects ungenerated revenue to recover its normal fixed costs associated with Noranda's class, demonstrates that this AAO is qualitatively different from those considered by the Commission in the past. Prior AAOs for ice storms have been authorized for the Commission in the past because ice storms occur erratically, and so, the sometimes great costs associated with the storms are difficult to normalize into rates through standard means. But those AAOs have been recovered in rates where the utility actually incurred some – extraordinary – costs as a result of the event and the Commission presumably has determined those costs should be put into rates in order to minimize the risk of under-recovery in the next period. Here, the record unequivocally demonstrates that Ameren had **no** costs related to the Noranda outage in the ice storm (Tr. Vol. 18, p. 71; see also Ex. 406, pp. 13-14). Moreover, the record unequivocally demonstrates that instead of storm costs, Ameren seeks to recover only known and anticipated "fixed costs" previously allocated in a rate case but *unrecovered*, another way of saying "lost revenues" (Tr. Vol. 18, p. 728; see also Ex. 4, p. 19).[3] As a result, there can be no dispute that this AAO is solely about lost revenue from a prior period that Ameren seeks to

[2] Again, it is not clear whether such an end can ever be accomplished using an AAO given that the standard for the AAO includes a requirement that the event be non-recurring.

[3] As MIEC and OPC assert in their respective Post-Hearing Briefs and MIEC's testimony, Ameren Missouri in fact did recover all of its fixed costs in the relevant period. The costs were recovered from other, non-LTS customers.

recover going forward.[4] Belated recovery of lost revenue is prohibited by law and the Commission must deny Ameren's request to recover the AAO in this rate case.

Finally, as noted in Public Counsel's Post-Hearing Brief, if recovery of the AAO in rates is lawful, whatever sum is set in rates still must be supported by the substantial and competent evidence in the record in this case (OPC Br. at 14). *Office of the Public Counsel v. Pub. Serv. Comm'n*, 409 S.W.3d 371, 375 (Mo. 2013).. Depending on the Commission's review of the record, the Commission could conclude that the record supports recovery of only some or none of the amount it previously authorized for deferral (Ex. 412, Report and Order, Case No. GR-98-140). The Commission's discretion in this regard is not limited to a prudence review or a mere examination of whether the mathematical calculations are correct. Rather, the Commission is obligated to undertake a broad examination of all the relevant factors necessary to set rates under the standard put forth in *UCCM*.

Return on Common Equity ("ROE")

The evidence shows that the Commission should accept Public Counsel's recommendation that Ameren Missouri's required return on common equity be set at 9.01%. Using Public Counsel's recommended return on equity of 9.01% as the cost of common equity along with the Company's capital structure and embedded costs of long-term debt, short-term debt and preferred equity, means a reasonable level of Ameren Missouri's weighted average cost of capital is 7.327% (Ex. 409, 410, 411).

On pages 55-56 of its Initial Brief, Ameren Missouri states:

> Both Mr. Gorman and Mr. Murray raise their recommended returns when considering the allowed returns from other jurisdictions, acknowledging (at least implicitly) that investors

> consider that information. Considering this evidence, Mr. Murray's and Mr. Gorman's estimates of required returns would be 9.5% and 9.63%, respectively. Mr. Schafer acknowledges other authorized returns in other jurisdictions, but attempts to minimize the implications of such results in comparison to his very low recommendation of 9.01%.

(footnote omitted). This is a well-worn tune played by Ameren Missouri. While recent authorized ROEs from around the nation are one factor to consider when setting an authorized ROE in this case, it is also important to note that this factor is not the only factor, or even the predominant one, as Mr. Hevert would have the Commission believe.

A reasonable return on equity, as developed by the U.S. Supreme Court is: (1) adequate to attract capital at reasonable terms, thereby enabling the utility to provide safe and reliable electric service; (2) sufficient to ensure the Companies' financial integrity; and (3) commensurate with returns on investments in enterprises having corresponding risks. *Bluefield Waterworks and Improvement Co. v. Pub. Serv. Comm'n of W.Va.*, 262 U.S. 679 (1923) ("*Bluefield*"); *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591 (1944) ("*Hope*"); Tr. Vol. 21 p. 1126, 1197). The first two factors focus on the intrinsic nature of setting a reasonable return on equity which would provide the utility financial integrity and the ability to attract capital, enabling it to provide safe and adequate service. The third factor focuses on the extrinsic nature of setting a reasonable return on equity with an eye to returns for investments of other similarly situated entities facing similarly situated risk as the utility.

In his rebuttal, Mr. Hevert questioned the overall reasonableness of Mr. Schafer's recommendation on the basis that it "falls well below the returns authorized recently for the vertically integrated electric utilities against which Ameren Missouri must compete for capital - it even falls well below the returns authorized for natural gas distribution utilities." (Ex. 17 p.

72). In other words, Mr. Hevert questions whether Mr. Schafer's recommendation takes into account the extrinsic information required by the third *Bluefield* and *Hope* factor of a reasonable ROE.

In fact, Mr. Schafer's analysis does take into account returns for investments of other similarly situated entities facing similarly situated risk as Ameren Missouri. Each of the return on equity experts utilized a proxy group in their analysis (Tr. Vol. 21 p. 1145). As Mr. Hevert agreed at the hearing, the main purpose in constructing a proxy group is essentially to try to, as closely as possible, approximate the profile of Ameren Missouri (Tr. Vol. 21 p. 1145). As such, a proxy group provides extrinsic information on similarly situated entities facing similarly situated risk as Ameren Missouri which is then used in traditional analytical tools to determine a reasonable ROE for Ameren Missouri. Therefore, every expert's use of a proxy group in their analysis is an attempt to meet the third *Bluefield* and *Hope* factor of a reasonable ROE.

But, the evidence clearly shows that three of the four experts have return on equity recommendations in the low 9% area while Mr. Hevert has an outlier recommendation of 10.4%. Trying to overcome this, Mr. Hevert goes on to set up his own test of ROE reasonableness which Mr. Schafer, Mr. Gorman and Mr. Murray not surprisingly all fail:

> Mr. Hevert compares all of the witnesses' recommended ROEs to a list of recently authorized ROEs for vertically integrated electric utilities. Noting that only his recommendation falls within the range of recently authorized ROEs, Mr. Hevert concludes that the "opposing ROE witnesses' recommendations [...] fail to meet that basic test of reasonableness," which implies that Mr. Hevert would find questionable any recommendation outside the range of his list of recently authorized ROEs. Additionally, Mr. Hevert applies the same test of "reasonableness" to individual results of financial models, noting, for example, that Mr. Murray's CAPM results have "no practical meaning" because they fall well below the "benchmark" of the average of his list of recently authorized ROEs.

(Ex. 411 *citing* Ex. 17). Essentially, Mr. Hevert's claim is that the opposing witnesses' recommendations fail a test of "reasonableness" because they do not correspond to ROEs of an historical period he determines. So, since we are still dealing with the effect of extrinsic data on a reasonable ROE, Mr. Hevert would have the Commission believe that the third *Bluefield* and *Hope* factor means if a ROE does not match some list of recently authorized ROEs that he created, then the ROE cannot be reasonable. Such an assertion is a distortion of what the law actually requires, which is setting a reasonable return on equity with an eye to returns for investments of other similarly situated entities facing similarly situated risk as the utility.

Still, Mr. Hevert persists with his own test of "reasonableness." For his assertion of reasonableness, Mr. Hevert presents the 2014 national average of allowed ROEs (through November), which is 9.96% (Ex.17). The range establishing this average is characterized by ROEs as low as 9.5% and as high as 10.95% (Ex. 17). It is important to note that the range is characterized by a spread of 145 basis points (10.95% - 9.50% = 1.45%). So, what the existence of such a wide range of authorized ROEs actually demonstrates is that regulators do not provide quite as much emphasis on this measure of purported comparative reasonableness that Mr. Hevert suggests they do.

The evidence also shows that Mr. Hevert makes two arguments regarding recently authorized ROEs that contradict his own conclusions (Ex. 17, 411). First, he argues that recommendations outside the range of recently authorized ROEs do not pass his determination of what is reasonable (Ex. 17, 411). Second, he argues that recommendations which fall below the average of historically authorized ROEs are not reasonable (Ex. 17, 411). However, when applied in a consistent manner this cannot be one of his criteria because one of the authorized

ROEs (10.95%) in the range on which Mr. Hevert relies is actually farther from the national average than all of the recommendations made by the opposing witnesses in this case (Ex. 411). What Mr. Hevert seems to be saying is that if the ROE is lower than average it must be discarded, but if it is higher than average it must be considered (Ex. 411). What this observation puts on display is that Mr. Hevert's analysis is misleading, and again, that his emphasis on this one particular factor is misplaced (Ex. 411). Additionally, common sense dictates that Mr. Hevert would apply the same test of "reasonableness" to his own analysis. But, as Mr. Schafer in his surrebuttal (Ex. 411) notes:

> No, he does not. However, if he did, eight of Mr. Hevert's 29 results (i.e., 27.6% of his results) would be considered unreasonable under the guidelines he has established. Five of his results would be too high; three of his results, too low.

Inconsistent application and failure to apply his own test to his own analysis most certainly calls into question the value of Mr. Hevert's test of "reasonableness" as necessary to meet the third *Bluefield* and *Hope* factor for a reasonable ROE.

Also, just because an ROE was reasonable in the past does not automatically mean it is reasonable today. According to the United States Supreme Court in *Bluefield*, 262 U.S. at 693, "a rate of return may be reasonable at one time and become too high or too low by changes affecting opportunities for investment, the money market and business conditions generally." As the *Bluefield* decision indicates, rate-of-return witnesses must account for changes in market data rather than perpetuate estimates that may have become too high or too low with time. If utility Commissions adopted Mr. Hevert's belief, they would value only those results that agreed with the past and, therefore, might unreasonably neglect current economic information.

Mr. Hevert's attempt to discredit the findings of the other three experts by placing undue emphasis on historical findings of utility commissions is unreasonable. Historical ROEs should not be used to determine whether a party's recommendation should be given more or less weight, nor is it a particularly strong indicator of what the correct outcome should be in this case. The results of rigorous, accepted financial models should not automatically be declared unreasonable because they fall outside an artificial range of authorized ROEs established by different regulators in divergent jurisdictions regulating distinct utilities over an arbitrary period of time. Moreover, were this Commission to authorize an ROE not falling within Mr. Hevert's artificial range, it does not then follow automatically that the ROE would be unreasonable. As a result, the evidence shows that Public Counsel's recommendation of Ameren Missouri's required return on common equity of 9.01% reasonably balances the interest of the customers with those of investors. Mr. Hevert's recommended ROE of 10.4% is excessive and should be rejected by the Commission.

Moreover, the evidence shows that three of the four experts have return on equity recommendations in the low 9% area which are based on analysis of market-driven data using traditional analytical tools. In its Initial Post-Hearing Brief, Ameren Missouri attempts to minimize this fact in order to bolster the outlier 10.4% ROE recommendation of Mr. Hevert. But the fact that three out of the four experts in this case have recommendations in the low 9% range cannot be ignored or brushed aside as Ameren Missouri would hope.

Public Counsel witness, Mr. Schafer, recommends a return on equity of 9.01% (Ex. 409, 410 & 411). This recommendation is the average of the three estimates Mr. Schafer calculates based on a Constant Growth Discounted Cash Flow (DCF) analysis, a Risk Premium analysis and the Capital Asset Pricing Model study, which show that a ROE between 8.74% to 9.22%

would be reasonable (Ex. 409, 410 & 411). Similarly, MIEC witness, Mr. Gorman recommends a return on common equity of 9.30%, which is at the midpoint of his recommended range of 9.00% to 9.60% (Ex. 510, 511, 512; Tr. Vol. 21 p. 1196). Mr. Gorman's ROE range is also based on his expert analysis of market-driven data through his use of a DCF analysis, a Risk Premium analysis and the Capital Asset Pricing Model (Ex. 510, Tr. Vol. 21 p. 1196-1197). Staff witness Mr. Murray presented a return on equity in the range 9.00% to 9.50%, with a recommendation of 9.25% (Ex. 202; Tr. Vol. 21 p. 1340-1341). This range also encompasses Mr. Schafer's recommended 9.01% ROE (Tr. Vol. 21 p. 1343). Mr. Murray's determination is also based on his expert analysis of market-driven data using traditional analytical tools (Tr. Vol. 21 p. 1341). Still, Mr. Hevert recommends an ROE of 10.4%, which is significantly higher than the 9.8% ROE Ameren Missouri was awarded in its last rate case (Tr. Vol. 21 p. 1288).

It is not surprising that Ameren Missouri has the highest recommended ROE of all the return on equity witnesses in this case. A utility has every incentive to seek the highest return possible for its shareholders. But, if the utility has a right to expect the Commission to increase its return on equity in a rate case if reasonable to do so, then customers have the right to expect the Commission to decrease the return on equity in a rate case if the evidence suggests it is the fair thing to do. In an attempt to shift the balance in favor of shareholders, Ameren Missouri provides an explanation on page 56 of its Initial Post-Hearing Brief for the vast difference between its witness and the other three return on equity witnesses:

> The disparity between prevailing returns and Staff, OPC and Intervenor recommendations is the result of limited inputs and a results-oriented pessimism that underlies key assumptions that drive the output of their models.

However, the Commission can easily find evidence that Ameren Missouri's own recommendation is the result of limited inputs and a results-oriented optimism.

As explained in Mr. Schafer's rebuttal testimony (Ex. 410), Mr. Hevert's results are unreasonably high because of the following factors:

- The use of "mean high" and "mean low" growth estimates
- A dividend payment timing error
- An inappropriate payout-ratio forecast
- An unreasonably high estimation of GDP
- Risk premia established with unreasonably high constant-growth rates
- The selective use of a "long term projected" risk-free rate
- An inappropriately applied argument relating to the supposed inverse relationship between interest rates and the equity risk premium

The following table summarizes Mr. Schafer's analysis and correction of Mr. Hevert's results (Ex. 410):

Mr. Hevert				
	Original Results			**Corrected Results with Updated Stock Prices and the Exclusion of Duke and Cleco**
Constant-Growth DCF	Mean Low	Mean	Mean High	Mean
30-Day Average	8.44%	9.56%	10.87%	**9.37%**
90-Day Average	8.50%	9.62%	10.93%	**9.53%**
180-Day Average	8.61%	9.73%	11.04%	**9.56%**
Multi-Stage DCF				

30-Day Average	9.61%	9.93%	10.36%		**8.84%**	
90-Day Average	9.67%	10.00%	10.43%		**9.00%**	
180-Day Average	9.80%	10.13%	10.58%		**9.03%**	
CAPM Results	Bloomberg Derived Market Risk Premium	Value Line Derived Market Risk Premium			6.2% Market Risk Premium	
Average Bloomberg Beta Coefficient						
Current 30-Year Treasury (3.42%)	11.27%	10.69%			**8.34%**	
Near Term 30-Year Treasury (4.07%)	11.92%	11.34%			**8.98%**	
Average Value Line Beta Coefficient						
Current 30-Year Treasury (3.42%)	11.17%	10.59%			**8.33%**	
Near Term 30-Year Treasury (4.07%)	11.82%	11.24%			**8.98%**	
Bond Yield Plus Risk Premium	**Low**	**Mid**	**High**		**Low**	**High**
	10.16%	10.31%	10.77%		**7.85%**	**8.50%**
Final Recommendation	10.40%				**9.07%**	

In his direct testimony, Mr. Hevert recommended a 40 basis-point range, the low estimate of which was situated at approximately the midpoint of his highest and lowest estimates (Ex. 16, 410). Correcting Mr. Hevert's low estimate results in a value of 8.18% which comes from the average result of the bond-yield plus-risk-premium approach ((8.50% + 7.85%) / 2) (Ex. 410). Correcting Mr. Hevert's high estimate results in a value of 9.56% which comes from the constant-growth DCF model (Ex. 410). The midpoint of the corrected high and low estimates is 8.87% ((8.18 + 9.56%)/ 2) (Ex. 410). Correcting Mr. Hevert's final recommended range would result in a range from 8.87% to 9.27%, with a midpoint final recommended ROE of 9.07% (Ex. 410). This result is much more in line with the results of the other three return on equity experts.

Mr. Schafer's analysis of Mr. Hevert's results provides the Commission a more appropriate view in order to equally balance the interests of the investor and the consumer as required by *Hope*, 320 U.S. at 603. But Ameren Missouri attempts to waive away Mr. Schafer's analysis by pointing out that this was his first time preparing this type of testimony:

> The Company fully recognizes that an expert witness has to begin at some point, and does not intend to denigrate Mr. Shafer in this regard. However, at this juncture, Mr. Schafer's limited experience indicates his analysis is academic in nature, and these facts should impact the weight to be accorded to it.

While a new witness may seem to be an easy target, the fact is that a fresh perspective brings its own insight and benefit to the process. Indeed, Mr. Hevert's own analysis could benefit from more of the "academic" rigor Mr. Schafer brings to his work and which Ameren puzzlingly derides.

Mr. Hevert has worked in regulated industries for over twenty-five years (Ex. 16) and has provided numerous rounds of testimony on rate of return issues *exclusively* on behalf of utilities (Tr. Vol. 21 p. 1144). Mr. Schafer comes to this case not with years of bias, well practiced litany or a desire to produce millions in profits for his client, but with the open perspective brought by rigorous academic training coupled with the credentials of a top-of-the-class student having passed the prestigious level one Chartered Financial Analyst exam. The results of Mr. Schafer's analysis are bolstered by the independent work of Mr. Gorman and Mr. Murray, both well respected veterans to this type of analysis, who provided reasonable ROE ranges which encompass Mr. Schafer's recommended 9.01% ROE (Tr. Vol. 21 p. 1198, 1343). So, the evidence shows Mr. Schafer produced top-notch analysis of market-driven data using highly sophisticated traditional analytical tools his first time out of the gate, and he did so without Mr. Hevert's bias-inducing billing rate of $350 an hour (Tr. Vol. 21 pg. 1144).

The evidence clearly shows that three of the four experts have return on equity recommendations in the low 9% area which are based on analysis of market-driven data using traditional analytical tools. Correcting Mr. Hevert's final recommended ROE would result in a recommended ROE of 9.07% (Ex. 410). As a result, the evidence shows that Public Counsel's recommendation of Ameren Missouri's required return on common equity of 9.01% reasonably balances the interest of the customers with those of investors. Mr. Hevert's recommended ROE of 10.4% is excessive and should be rejected by the Commission.

Trackers

Rather than offering any substantive support for the continuation of any of the cost trackers at issue in this case, the company attempts to justify continued use of a tracker because the parties opposing the trackers – every party except the Company – appear to have a generalized dislike for deferral mechanisms.[5] Of course, this argument is not a substantive reason for the Commission to authorize a tracker. Parties *should* dislike deferral mechanisms. Any mechanism that creates a timing distortion between costs and revenues creates a matching principle problem and creates a false picture of the company's overall level of costs. Certainly when setting rates an accurate picture of Ameren Missouri's finances is vital.

Neither is the Company's assertion that a tracker is beneficial to customers a valid argument. No party except the Ameren Missouri believes that trackers benefit customers. Under the regulatory compact, customers benefit when the Company has an incentive to seek efficiencies and control costs. Every party except Ameren knows that trackers reduce a company's incentive to control costs. The Commission has repeatedly affirmed this fact. In ER-

[5] Ameren makes this claim, even though Staff offered testimony that an alternative to the tracker is the use of an AAO – which is itself a deferral mechanism.

2010-0036, the Commission denied Ameren's request for storm tracker authorization, explaining: "…trackers should be used sparingly because they tend to limit a utility's incentive to prudently manage its costs." Report and Order, ER-2010-0036, p. 66 (May 28, 2010) (Doc. No. 759). Even when authorizing a tracker, the Commission has expressed its disfavor:

> In general, the Commission remains skeptical of proposed tracking mechanisms. There is a legitimate concern that a tracker can reduce a company's incentive to aggressively control costs.

Report and Order, ER-2012-0166, p. 96 (Dec. 12, 2012) (Doc. No. 553). Rather than desiring to benefit customers, the real reason Ameren seeks authorization for trackers is to reduce its own risk. As the Company is able to shift more and more risk to ratepayers, the customers lose the benefit of the regulatory compact. Being forced to bear more risk does not benefit customers. If the Commission chooses to authorize a tracker, it should do so only when justified by extraordinary circumstances. Ameren has failed to provide any compelling reason the requested trackers should be re-authorized.

Storm Cost Tracker

Ameren argues a storm cost tracker should be continued because: 1) Ameren has no control over when storms occur and little ability to control restoration cost, 2) Ameren has a consistent record of spending money prudently when restoring service in the past, and 3) under traditional modes of regulation storm costs can have a significant impact on the company's ability to earn a reasonable rate of return. None of these reasons merits re-authorization of a storm cost tracker.

First, storm costs are a normal and ongoing expense for an electric utility. Variation in the level of storm costs incurred is not distinct from many other costs the Company incurs (Ex. 408, p. 8). Traditional ratemaking methods have enabled the company to recover its storm costs

adequately. Ameren's witness Mr. Wakeman testified that Ameren has never had any expense disallowed during major storms (Tr. Vol. 20, p. 839). Second, the fact that Ameren has spent money prudently when restoring service in the past is not a reason to depart from traditional ratemaking methods. If the Company incurred imprudent costs, those costs should be disallowed. Yet, past prudence does not provide any assurance that costs will continue to be prudently incurred in the future. Third, storm costs have not had a significant impact on the Company's ability to earn a reasonable return, and so, do not justify a special tracker. Ameren recovered all storm restoration costs prior to having a storm tracker mechanism (Tr. Vol. 20, p. 851). Further, the annual amount for storm restoration costs is less than 2/10ths of 1% of the Company's total operating expenses (Ex. 408, p. 10). The Company has recovered its storm cost so there is no threat to the company's ability to earn a reasonable rate of return. In addition, the Company's mathematical formula to determine the storms for which costs can be recovered through a tracker may create a disincentive to respond quickly. If IEEE Standard 1366 relies on how long customer service is interrupted as the basis for determining whether or not a storm qualifies as a major storm, and if major storm restoration costs can be recovered in the tracker, then use of Ameren's formula may create a disincentive to respond quickly to customer outages in order to ensure a storm qualifies as major and that costs can be recovered in the tracker.

Vegetation Management and Infrastructure Inspection Trackers

Ameren's reasons for continuation of the vegetation management and infrastructure inspection trackers fail to provide a rational basis for re-authorizing the mechanism. The Commission initially authorized these trackers to benefit the Company in a period if transition between when new rules were implemented and when enough historical cost data had been collected to develop a cost level in future cases. When authorizing the trackers in 2008, the

Commission stated that it "…does not intend to allow the overuse of tracking mechanisms in this case or in future cases." Report and Order, Case No. ER-2008-0318, p. 41 (Jan. 27, 2009) (Doc. No. 589). Later in 2012, the Commission allowed the continuation of the trackers but made clear that it did "…not intend for this tracker to become permanent." Report and Order, ER-2012-0166 at 106-07. The parties opposing the tracker in this case offered testimony that the purpose of the tracker has been fulfilled and that this risk-shifting mechanism is no longer needed.

Despite the clear language from the Commission's previous orders, Ameren requests continuation of the trackers. However, rather than substantively arguing that the purpose of the trackers has not been fulfilled – because Ameren cannot – Ameren asks the Commission to reject the arguments of the other parties. In addition to ignoring its burden to show why the tracker is needed, Ameren's arguments are unconvincing. First, Ameren repeats that each party opposes the trackers because of a "generalized dislike for, and opposition to, deferral mechanisms." (Ameren Br. at 117). The fact that parties may or may not generally oppose the use of trackers as a matter of policy has no bearing on whether or not the Company has put forth substantive evidence that a tracker should be re-authorized here. Second, Ameren argues that the parties ignore the fact that the costs to comply with vegetation management and infrastructure management fluctuate year to year beyond the company's control (Id.) Public Counsel agrees that costs fluctuate, the same as many other costs the company incurs. However, mere fluctuation does not justify continued use of a tracker. A sufficient historical database of actual costs exists upon which to determine an annualized level of costs to include in the development of rates (Ex. 408, pp. 15-16). Third, Ameren claims that the parties ignore the language of the rules that allow trackers to be used to track the compliance costs associated with the vegetation management and infrastructure inspection rules (Ameren Br. at 117). The issue in this case is whether the trackers

should be continued, not whether the trackers should have ever been authorized. The testimony in this case shows that the trackers are no longer necessary. There is nearly seven years of data upon which the Commission can rely for setting a base level of costs in rates (Ex. 406, pp. 30-31). The Company has completed full cycles for both the vegetation and infrastructure trackers (Ex. 217, p. 8). Public Counsel does not ignore the language of the rules that allowed trackers. Instead, Public Counsel has offered evidence that these trackers are no longer needed.

Ameren's arguments regarding the cost trends for vegetation management and infrastructure inspection are flawed. For vegetation management costs, Ameren states "Overall, compliance costs have shown a marked upward trend over the period 2008 through the end of the true-up period in this case." (Ameren Br. at 117). Simply because the costs are higher in the test year than during the first year of the tracker, the Commission should not infer that the costs will continue to increase. Public Counsel's Ted Robertson provided testimony that provides the rest of the story:

> For the five preceding twelve-month periods ending in March, the Company's actual vegetation management expense has been somewhat variable, both up and down, within a range of $48,858,868 to $56,289,626. In year two the expenses decreased to $48,858,868 from the year one amount of $51,349,250. In year three the actual expense increased to $55,515,566 and then decreased to $50,520,899 in year four.

(Ex. 408, p. 13). Notably, Mr. Robertson's amounts are different from the amounts used in the chart cited by Ameren in its brief. This is because Mr. Robertson uses data from twelve-month periods ending in March – corresponding with the test year in this case – while the chart included in Exhibit 513 shows the calendar year totals for each expense (*See* Ex. 513, p. 18). Since rates are set using the test year, the amounts provided in Mr. Robertson's testimony are preferable. Rather than showing a consistent increase in costs, the data shows that the costs for vegetation

management have fluctuated up and down (Ex. 408, p. 13). Because of this variability, the best ratemaking methodology to determine a cost level going forward is to normalize the costs based on an average of the actual historical costs (Ex. 408, p. 13). A tracker is simply not needed.

The Company's contention that annual expenditures for infrastructure inspection have increased each year since 2012 is wrong. With the exception of the test year, infrastructure inspection costs have decreased (Ex. 408, p. 14). Mr. Robertson's testimony included an examination of the cost trend for infrastructure management costs:

> For the five preceding twelve-month periods ending in March, the Company's actual infrastructure inspection expense has decreased in all years except for the twelve months ended March 2014. In the first year the expenses were $8,165,926 while in year four they were $5,373,259 – a decrease of $2.8 million. For the twelve months ended March 2014, the actual incurred expense was $5,924,356 – an increase of only $551 thousand over year four. These costs have shown a clear and substantial decreasing trend in all years except the test year.

(Ex. 408, p. 14). Based on the testimony of Mr. Robertson using data that corresponds to the test-year time frame, the costs for infrastructure inspection generally have decreased. With costs generally decreasing, any possible remaining need for a cost tracker is eliminated.

For both the vegetation and infrastructure trackers, Ameren has failed to provide any substantive argument in favor of continuation. Enough historical data exists at this point so that a tracker is no longer needed to protect the company from unknown and uncertain costs of complying with new Commission rules. Discontinuing these extraordinary trackers will restore an appropriate balance of risk back to the company and is in the public interest.

Street Lighting

The Cities of O'Fallon and Ballwin ("the Cities") request that this Commission require Ameren Missouri to revise its 5(M) (utility-owned street lighting) termination tariff so that they

may migrate to Ameren's 6(M) (customer-owned street lighting) tariff. The Cities suggest that movement to the 6(M) tariff will permit O'Fallon to reduce annual costs on street lighting by approximately $820,000 annually and Ballwin to reduce its annual street lighting costs by approximately $406,000 annually (Cities' Post-Hearing Brief at 1-2). To the extent the result of the Cities' request will be increases in rates on other customers, either intra-class or inter-class, the Commission should proceed with caution.

If the Commission is inclined to deny the Cities' request, the Commission could consider ordering the parties in the next rate case to disaggregate the "lighting class" in their respective Class-Cost-of-Service Studies in order to facilitate a potential revenue-neutral adjustment among the different lighting customers. In this case, Ameren concludes that rates for the 5(M) class need to decrease by 11% to reach cost of service using its methodology (Tr. 1841-1843; Ex. 9, pp. 40-41). OPC has no position whether Ameren's calculations are correct in this case, and Staff has taken no position on the question (Staff Br. at 88). However, the Commission may conclude that the next rate case is the time for a deeper examination of this question and such a decision would have the benefit of permitting the parties to develop a full record for the Commission's consideration.

Class Cost of Service, Revenue Allocation and Rate Design

Public Counsel's positions with respect to revenue allocation and rate design are reflected in the Non-unanimous Stipulation and Agreement ("Stipulation") regarding rate design and other matters entered into by various consumer parties in this case (Doc. No. 436). In short, the stipulating parties recommend: 1) retention of the residential customer charge at $8.00 per month, 2) no revenue-neutral inter-class adjustment in this case, and 3) application of any

revenue requirement increase on an equal proportion basis across all existing classes, among other provisions.

Customer Charge

With respect to the customer charge, it is heartening to see Ameren Missouri concede in its Initial Post-Hearing Brief that in this case the increase proposed by the Company will have no effect on the energy conservation price signal sent to consumers (Ameren Br. at 152). As a result, the facts in this case do not demand that the Commission re-plow old policy ground concerning customer charges and energy conservation. Instead, the Commission can focus on the nuts and bolts of cost-causation and allocation. Where the customer charge is concerned, the best evidence of cost-causation before the Commission in this case comes from Staff. This is so because Staff lacks the obvious bias towards shifting business risk onto the backs of customers that Ameren Missouri plainly has.

According to Staff, a customer charge of $8.11 is appropriate if the only consideration before the Commission in setting the charge is the result of a class-cost-of-service study (Staff Br. at 80). Staff's cost study appropriately limits those costs for inclusion in the customer charge to those that are directly attributable to the incremental additional cost of adding each new residential customer – meter reading, bill postage, etc. (Staff Br. at 80-81). Ameren suggests that adding some portion of the cost of the distribution system to the customer charge is appropriate (Ameren Br. at 151). Staff, and prior Commissions, have rejected this drastic expansion in the scope of the customer charge cost allocation (Staff Br. at 81). And interestingly, instead of following the findings of its own (wrong) cost study, Ameren deviates substantially from the cost of service identified in its own study and recommends only a percentage increase to the customer

charge equal to any revenue requirement increase secured in the case.[6] Of course in making this recommendation to deviate so substantially from the results of its own cost of service study, consistency with which Ameren asserts is of paramount importance when considering Noranda's rate request, Ameren lays bare the inconsistencies of its own positions and reinforces why the Company has a complete lack of credibility on the Noranda matter with consumers.

Staff also suggests deviating from the results of its cost of service study, but not to the great degree Ameren suggests for the customer charge, and makes its suggestion in recognition of the import the Commission typically places on facts such as rate continuity, customer acceptance, prior policy determinations keeping the customer charge low, and the like.[7] As a result, Staff recommends maintaining the customer charge at its current $8.00 per month rate. OPC fully supports Staff's position on this issue.

Revenue-Neutral Inter-Class Cost Shift

Again, Public Counsel's position on this question is resolved through the consumer rate design Stipulation filed in this case. However, a few points should be addressed in reply to support the reasonableness of the Stipulation's resolution of this issue.

As a preliminary matter, the results of the various class-cost-of-service studies merit discussion. But perspective is important on the utility of the studies. The Midwest Energy Consumers' Group desires this Commission to consider the class-cost-of-service study to be something akin to the Holy Grail of cost allocation. However, the record and law make clear that

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[6] Presumably Ameren Missouri would not suggest such a methodology for setting the customer charge if a revenue requirement decrease were indicated by the facts of this case.

[7] It should also be recognized that Staff's position with respect to the proper use of the cost study in the context of the all relevant factors analysis required by law is much more consistent throughout this case than Ameren's.

the CCOS is nothing so profound. As Staff rightly suggests, class-cost-of-service studies are merely one tool in the Commission's toolbox to determine how to allocate revenue requirement to customers (Staff Br. at 77-78; see also Tr. Vol. 35, pp. 3022-23). Additional considerations must also be balanced with the results of the class-cost-of-service studies in the record in order to come to a just and reasonable result.

In this case, various parties – usually parties aligned with comparatively high-load-factor and/or high-usage customers, or those with an interest in selling power to those customers – have attacked the use of OPC's preferred Peak and Average study. Such arguments should be seen by the Commission for what they are, self-serving. Unlike any other study offered by the Commission in this case, OPC's Peak and Average study does not provide undue cost-subsidy for the high-load-factor, high-usage customer. Instead, the Peak and Average study utilizes an entirely different methodology, a methodology that gives due and appropriate consideration to low-load-factor and/or low-use customers.

OPC recognizes the Commission's prior statements with respect to the Peak and Average study, and in recognition of those statements OPC submitted its second Average and Excess study. OPC's Average and Excess study reflects its view of the appropriate allocations of costs among the classes using a methodology approved of by the Commission in Ameren's last rate case. But this Commission should not simply ignore the results of the Peak and Average study if it declines to follow the Stipulation. Rather, the Commission should then recognize that the Peak and Average methodology is generally-accepted in the field and balances the record in this case by providing the low-use, low-load-factor (residential) customer perspective on rate design that is lacking from the other parties' submissions. And the perspective of the low-use, low-load-factor customers afforded to the Commission by the Peak and Average study is a factor to weigh

- an important one - when determining: 1) class cost of service in this case, 2) whether any revenue-neutral inter-class adjustment is merited by the substantial and competent evidence, and 3) if merited, the degree of the shift which may be just and reasonable.

In recommending no revenue-neutral shift to the Commission, the Stipulation takes into account the whole record before the Commission, including the factors supporting and opposing the perspectives of both the low- and high-load customers both an inter- and intra-class basis. Ultimately, the signatories to the Stipulation found that its terms balanced those factors acceptably, and that the terms struck an acceptable balance amongst each other such that the agreement as a whole leads to a just and reasonable resolution of the issues treated therein.

New Revenue Requirement Allocation

In addition to Public Counsel's representation of all customers as a class, the signatories of the Stipulation represent a broad array of customers from every customer class except lighting.[8] Within the Stipulation, the customers find some common ground with Ameren. The stipulating parties agree that the increase in revenue requirement which may result from this case should be applied to all existing classes on a system-average, equal-percentage basis. Further, both MECG and Wal-Mart also concur that "any rate increase authorized in this case should be applied to all the classes on an equal percentage basis" (MECG Br. at 49 (citing Ex. 750, p. 9)).

Noranda Rate Proposal

OPC did not support an effective rate of $32.50 per MWh for the LTS class as proposed by Noranda in this case. Nor did OPC support Noranda's request for an effective rate of $30.00 per MWh in the rate design complaint case. Only under the terms and conditions articulated in the rate design Stipulation filed by various consumers in this case can OPC support a rate of

[8] Intervening lighting class representatives in this case did not file an objection to the Stipulation.

$34.00 per MWh for Noranda. Only with the existence of those strong consumer protections and other binding commitments from Noranda does OPC believe the relevant factors could support a $34.00 rate. Without those provisions, provisions which are impossible to secure in any wholesale arrangement even if such an arrangement were legal, any reduction of this magnitude in Noranda's rate is just a shift in cost from one customer to others with insufficient benefit to the others. And because the Stipulation contains strong consumer protections, will ensure Noranda continues to make a positive contribution to fixed costs going forward, will avoid an even larger cost shift onto other consumers if Noranda were to leave Ameren's system, and will provide substantial ancillary benefits to the state, OPC strongly supports it.

Ameren's Wholesale Proposal

First, it is important to note that Ameren Missouri's rate proposal represents a substantial concession on the part of Ameren. In making its proposal, Ameren for the first time offers to acquiesce to a reduction in Noranda's rates. However, Ameren's proposal is entirely incongruous with its other arguments with respect to Noranda's request – arguments Ameren does not back down from even in making its offer to give Noranda an effective rate reduction.

Missouri law prohibits Noranda from taking wholesale power.[9] Mo. Rev. Stat. § 91.026 (Cum. Supp. 2013). So, in order for Noranda to take advantage of Ameren's offer, an intermediary shell or front company would be needed to serve as a conduit for the parties to facilitate this otherwise illegal transaction. Ameren admits as much (Tr. Vol. 35, p. 2950-51). In creating this structure, however, nothing about Noranda's character as a retail customer will, or can, change, and just as importantly, nothing about Ameren Missouri's underlying costs to

[9]Of course, if the statute authorizing Noranda to change electric suppliers is unconstitutional, this issue can never be reached.

generate, transmit and distribute electricity to Noranda will change. Ameren has admitted this, too (Tr. Vol. 35, p. 2958-59). Further, inherent to Ameren's proposed deal, is that Noranda will pay a rate lower than what it currently pays, and one the Company admits will be lower than the cost to serve Noranda (Ex. 26, p.32). The only logical conclusion then, is that what Ameren is calling a wholesale proposal, is nothing of the sort as applied. Rather, it is a particularly convoluted and illegal proposal designed to offer Noranda a retail discount without directly backing down on its cost of service argument.[10] And like any retail cost shift, the incremental difference in the price Noranda now pays and what it would pay under this agreement would be borne entirely by Ameren's other ratepayers. The wholesale patina Ameren paints on its proposal is, like any patina, easily removed, and the underlying structure revealed for what it is, which in this case, is Noranda taking service at retail with no change in cost structure to support the new rate. From a fundamental perspective then, Ameren's proposal reflects Ameren's willingness to provide Noranda what is effectively a retail discount, one which is a deviation from Ameren's argument regarding cost of service, one which deviates from Ameren's assertions that it is acting to "protect" its customers, and despite the fact that Ameren believes Noranda does not actually need the discount.[11]

With that in mind, as a practical matter implementation of the proposal Ameren put forth belatedly in this case, even if it were legal, cannot move forward. The parties have no agreement, and it appears they never will. This Commission cannot mandate the parties enter into such an

[10] The proposal also is a transparent effort to divorce Noranda from any future interest in Missouri's regulatory and legislative environment.

[11] It is puzzling why any party would be willing to give Noranda a rate reduction below cost of service when that party does not believe that, but for the reduction, Noranda will no longer take load.

arrangement, nor can this Commission legally or practically incentivize such an arrangement. Further, any resolution to Noranda's request that fails to deal with the matter fully within this rate case unreasonably adds risk for all the parties that the relief requested will come too late to permit the New Madrid smelter to survive. Accordingly, OPC submits that the only avenue forward is for the Commission to determine: 1) whether or not Noranda needs a retail rate reduction in order to remain on Ameren's system, 2) if so, what retail rate is appropriate to preserve Noranda's load while remaining a benefit to Ameren's other customers, and 3) what terms or conditions should attend Noranda's receipt of that reduced rate.

This Commission lacks jurisdiction over wholesale power contracts, as it knows. *See New York v. Fed. Energy Reg. Comm'n*, 535 U.S. 1, 19-21 (2002); *Federal Power Comm'n v. Southern Cal. Edison Co.*, 376 U.S. 205, 215 (1964); 16 U.S.C. § 824(c)(d). Further, this Commission cannot establish itself as a gatekeeper or obstacle purporting regulating access to areas in which jurisdiction is occupied by federal authorities. *See generally Crosby v. Nat'l Foreign Trade Council*, 530 U.S. 363, 372 (2000); *Edgar v. Mite Corp.*, 457 U.S. 624, 631 (1982). The Commission cannot sanction an unlawful collateral attack on a prior commission order. Mo. Rev. Stat. § 386.550 (2000). The Commission cannot cancel or suspend a certificate of convenience and necessity under the conditions contemplated by this case. *State of Missouri* ex rel. *City of Sikeston v. Pub. Serv. Comm'n*, 82 S.W.2d 105 (Mo. 1935). The Commission is not empowered by the statute authorizing the fuel adjustment clauses to permit its use in the manner suggested by Ameren Missouri. Mo. Rev. Stat. § 386.266. And even if OPC is wrong and the Commission can do any or all of these things, it should not.

Ameren Missouri has no financial exposure to Noranda's request for relief in this case. Ameren suggests it has objected to Noranda's ask in order to preserve the principle of cost-of-

service ratemaking and protect its customers, but as the record in this very case shows, Ameren will deviate profoundly from these noble objectives when it thinks doing so is in its own best interests. Instead, it is far more likely that Ameren objects to Noranda's request strategically in an attempt to lever from Noranda concessions on a number of other regulatory and legislative issues, or to put it out of business.[12] In order to appear reasonable, Ameren then posits a "solution" to the dispute it created, but the solution it offers is one no party but Ameren finds acceptable.

The Stipulation agreed upon by various consumers parties may be imperfect, but it is reasonable in the judgment of those agreeing to it and, hopefully, in the Commission's judgment as well. As imperfect as some parties may find the Stipulation, it at least has the virtue of being agreed upon by more than one party to this case, importantly the parties who would actually pay the cost associated with it, and moves the case beyond the "my-way-or-the-highway" approach taken by some which has prohibited progress to date.

Questions of Commissioner Hall

To distill and recapitulate the points made by Public Counsel both in its Post-Hearing Brief and herein as it relates to the questions posed by Commissioner Hall, Public Counsel offers as follows:

A. What is the risk concern that Ameren and Noranda have with respect to the Wholesale Agreement proposal put forth by Ameren?

Public Counsel will defer to Ameren and Noranda to articulate their specific concerns about accepting the risk of the proposal. Many of Public Counsel's concerns with respect to the

[12] Ameren suggests it is not trying to put the New Madrid smelter out of business, but the result of its intransigence may lead to just that result if the Commission permits it.

legality of the proposal are articulated in its briefs. Those concerns may or may not be shared by Ameren and/or Noranda. Public Counsel can only speculate that the likelihood of success of one or more of the legal infirmities the parties identified in their own reviews of the arrangement, which may or may not be the same infirmities identified by Public Counsel, led neither of them to be willing to accept the financial consequences if the arrangement were invalidated.

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

Public Counsel does not believe it is possible for the Commission to mitigate or eliminate the risks identified by Public Counsel. Because the risks Public Counsel identified are not intrinsic to the transaction, but are constitutional and/or statutory in nature, they fall outside the authority of the Commission. Again, Noranda and/or Ameren may have a different perspective depending upon the particular risks identified by those parties.

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

Any risk that is based on the language of Missouri's statutory scheme can be ameliorated through a change in that language when such a change is consistent with the US and Missouri constitutions. However, given the evidence with respect to Noranda's financial status and the need for rate relief to facilitate certain future financial transactions, as a practical matter a legislative option would appear to come too late to provide the relief required to retain service. Moreover, not every risk factor – or perhaps even the most salient risk factors – can be resolved through action in the Missouri General Assembly.

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

To be sure, Noranda is prohibited by law from taking wholesale service. Under Ameren's proposal, Ameren and Noranda would negotiate a "wholesale" rate for service using a front company. Such a rate would be below Ameren's allocated, embedded cost to serve Noranda. Because nothing in Ameren Missouri's underlying cost structure to serve Noranda would change, the revenue requirement also would not change. Accordingly, the difference between those rates would be borne by all of Ameren Missouri's other ratepayers when they had no opportunity to negotiate that level of subsidy and no opportunity, even if legal in a FERC-regulated wholesale contract, to ensure certain consumer protections and conditions are applied in exchange for the subsidy.

Moreover, to the extent the price fixed in the contract negotiated exclusively between Ameren and Noranda was wrong, Ameren's proposed use of the Fuel Adjustment Clause would hold Ameren harmless from any loss. Rather, the cost difference between the contract price and the market price would be borne by Ameren's customers.

There is nothing the Commission can do within the Commission's authority to avoid these potential harms. The Commission cannot mandate the parties agree to a wholesale contract. The Commission cannot regulate the terms of a wholesale agreement. The Commission cannot thwart a wholesale contract by setting itself up as a gatekeeper and determine the preconditions which must be met before the parties may enter into a wholesale contract.

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

The Office of the Public Counsel has entered into a Stipulation wherein it agreed for this case not to oppose retention of what has been called the "N Factor."

D. Assuming that the AAO granted to Ameren for the ice storm that shut down Noranda was appropriate and was for lost fixed costs, what legal basis is there for denying recovery of those amounts deferred?

The *UCCM* case is not permissive; it requires disallowing recovery of the amount associated with the Ice Storm AAO. By characterizing the "fixed costs" as lost, Ameren concedes its request is actually about ungenerated revenue. Revenue which was expected but not generated in a prior period is not recoverable in a future period. Historical costs provide an important gauge from which to set prospective rates so as to ensure a reasonable likelihood that the utility will not under- or over-earn. However, the very nature of any AAO suggests that the event giving rise to the deferral is so extraordinary that it cannot be used to assist in setting rates prospectively. And this AAO in particular, dealing not with any added or unanticipated costs from the ice storm but instead ungenerated revenue, clearly violates the Court's guidance in *UCCM* defining retro-active ratemaking.

Conclusion

WHEREFORE, Public Counsel respectfully submits its Reply Brief in the above-captioned matter.

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned certifies that on this 10th day of April, 2015, a true and correct copy of the foregoing was served by US mail, postage prepaid, or by electronic delivery addressed to all parties by their attorneys of record.

/s/ Dustin J. Allison