BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Union Electric Company d/b/a AmerenUE for Authority to File Tariffs Increasing Rates for Electric Service Provided to Customers In the Company's Missouri Service Area.	))))	**Case No. ER-2008-0318**

AMERENUE'S RESPONSE TO APPLICATIONS FOR REHEARING AND MOTION FOR STAY

COMES NOW Union Electric Company d/b/a AmerenUE (AmerenUE or the Company) and, in compliance with the Commission's Order Establishing Time to Respond to Applications for Rehearing and Motion for Stay, and Directing Staff to File Recommendation Regarding Tariff, hereby responds to the Applications for Rehearing of the Office of the Public Counsel (OPC), AARP, and Noranda Aluminum, Inc. (Noranda), and also responds to Noranda's Motion for Stay.[1] For its response, AmerenUE states as follows:

I. The Law Governing the Commission's Authority in Setting Rates

A. The commission's charge in a rate case is to establish just and reasonable rates based upon the utility's cost of service.

Noranda in particular seeks to justify its rehearing application on bases that have nothing whatsoever to do with the Commission's statutory and constitutional duty to set just and reasonable rates. The Commission's authority in this area is based upon the cost of service ratemaking principles that have governed the Commission's exercise of its jurisdiction for nearly 100 years, as described at pages 7 to 11 of the Report and Order.

Instead, Noranda asks the Commission to assume a role only the Missouri General Assembly (or the United States Congress, as appropriate) can lawfully assume; that is, Noranda

[1] Unless otherwise noted, references herein to Noranda's rehearing application are intended to respond to Noranda's Motion for Stay as well, which is essentially premised on the asserted validity of the arguments it makes in its rehearing application.

asks the Commission to address broad social and economic policy for the State by artificially gerrymandering the ratemaking process to somehow solve the economic problems of private business and citizens occasioned by the current recession.[2] The Commission's job is not to address economic problems caused by recession; indeed, it is not within the Commission's power or authority to do so.[3]

As the Missouri Supreme Court has stated:

> The enactment of the Public Service Act marked a new era in the history of public utilities. Its purpose is to require the general public not only to pay rates which will keep public utility plants in proper repair for effective public service, but further to insure to the investors a reasonable return upon funds invested. The police power of the state demands as much. We can never have efficient service, unless there is a reasonable guaranty of fair returns for capital invested. The woof and warp of our Public Service Commission Act bespeaks these terms. The law would be a dead letter without them, and a commission under the law, that would not be the law in the proper spirit, would be breathing into*345 it the flames of ultimate deterioration of public utilities. These instrumentalities are a part of the very life blood of the state, and of its people, and a fair administration of the act is mandatory. When we say "fair," we mean fair to the public, and fair to the investors.[4]

The Commission, citing *Bluefield Water Works & Improvement Co. v. Pub. Serv. Comm'n of the State of West Virginia*, 262 U.S. 679, 690 (1923), itself recognized essentially these same principles in the Report and Order in this case:

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[2] Noranda would likely argue, and perhaps does argue, that given the recession the Commission should in effect act unconstitutionally and set rates that do not give AmerenUE a reasonable opportunity to earn a fair return insofar as AmerenUE has a monopoly service tereritory. Noranda seems to imply that AmerenUE's status as a monopoly provider of electric service is somehow unfair given that Noranda does not operate in a monopoly environment. What Noranda ignores, of course, is that in exchange for that monopoly service territory, AmerenUE's rates and its return and indeed most aspects of its business are highly regulated, and that AmerenUE has an obligation to serve all who are within its service territory and to provide them with safe and adequate service. That obligation carries with it, however, the constitutional right to a fair opportunity to earn a reasonable return; i.e, to rates that are just and reasonable and not confiscatory.

[3] The Commission's lack of authority to ignore the ratemaking process was acknowledged by Staff Counsel Thompson during this case: "And we all know, being engaged in this business as we are, that electric is a rising cost utility. That's what Mr. Lowery told you, and it's true. Every year it costs more to produce the same kilowatt. Every year. That means inevitably that there is a class of customers who are being priced out of the market. *Now, that's not an issue that this Commission can solve. That is a legislative issue"* (emphasis added). Tr. p. 70, l, 7-14.

[4] State ex rel. Washington Univ. v. Public Serv. Comm'n, 272 S.W. 971, 973 (Mo. banc 1925).

> Rates which are not sufficient to yield a reasonable return on the value of the property used at the time it is being used to render the services are unjust, unreasonable and confiscatory, and their enforcement deprive the public utility of its property in violation of the Fourteenth Amendment.[5]

B. Neither Noranda, OPC nor AARP establish any lawful grounds upon which rehearing can be granted.

The rehearing applications of OPC, AARP and Noranda are noteworthy in that they all almost entirely lack any citation or indeed any discussion of any of the law that governs the Commission's regulatory and ratemaking jurisdiction. They also fail to acknowledge the regulatory discretion possessed by the Commission,[6] or the standard of review that governs the lawfulness and reasonableness of a Commission's rate case order. The conspicuous lack of any governing law to support their rehearing applications is not surprising, given that the governing law is squarely against them on each and every point they raise.

Indeed, their arguments are largely a re-hash of arguments they have made throughout this case. Those arguments must be judged in reference to the following two questions. First, was the Commission's decision lawful (i.e., did the Commission have statutory authority to do what it did), and second, if the decision was lawful, was the decision reasonable?[7] This is the standard that courts will apply to the Commission's decision on review. A decision is lawful if the Commission had the statutory authority to act as it did.[8] There is no claim that the

[5] Nor can the Commission fail to "give heed to all legitimate expenses that will be charges upon income during the term of regulation." *West Ohio Gas Co. v. Public Utilities Comm'n of Ohio*, 294 U.S. 63, 71 (1935).
[6] *See, e.g.*, page 11 of the Report and Order, where the Commission itself discusses this discretion.
[7] *Id.; see also State ex rel. Atmos Energy Corp. v. Pub. Serv. Comm'n*, 103 S.W.3d 753, 759 (Mo. banc 2003)*; State ex rel. Alma Tele. Co. v. Pub. Serv. Comm'n*, 40 S.W.3d 381, 387 (Mo. App. W.D. 2001).
[8] *Friendship Village*, 907 S.W.2d at 344.

Commission lacks statutory authority to determine a revenue requirement, set rates, and approve a rate design respecting the recovery of the revenue requirement.[9]

As to matters of reasonableness, the courts determine whether the order was supported by substantial and competent evidence on the whole record, whether the decision was arbitrary, capricious, or unreasonable, or whether the Commission abused its discretion. *Id.* An abuse of discretion would only occur if the Commission's decision is clearly against the logic of the circumstances then before it and is so arbitrary and unreasonable as to shock the sense of justice and indicate a lack of careful consideration.[10] If reasonable people can differ about the propriety of the Commission's action, then it cannot be said that the Commission abused its discretion.[11] A decision would only be arbitrary and capricious if it was the result of willful and unreasoning action, "without consideration of and in disregard of the facts and circumstances . . .."[12] It is obvious that OPC, Noranda and AARP "disagree" with the Commission's decision, but they fall far short of establishing that the decision does not rest upon substantial and competent evidence, was unreasonable, or constitutes an abuse of the Commission's discretion.

Moreover, a Commission order is presumed correct; the burden of proving its invalidity is on those attacking it.[13] Courts will review the evidence in the light most favorable to the Commission's decision along with all reasonable supporting inferences, and will defer to the

[9] As we will address below, Noranda raises one question about the Commission's authority; that is, Noranda claims that the S.B. 179 (Section 386.266, RSMo. (Cum. Supp. 2008)) does not in fact allow the Commission to adopt a fuel adjustment clause (FAC). Noranda's argument has been rejected by the Missouri Court of Appeals, as we will explain below.

[10] *Bowman v. McDonald's Corp*, 916 S.W.2d 270, 276 (Mo. App. W.D. 1995), *citing Egelhoff v. Holt*, 875 S.W.2d 543, 549-50 (Mo. banc 1994); *Richardson v. State Highway and Transportation Comm'n*, 863 S.W.2d 876, 881 (Mo. banc 1994).

[11] *Id.*, *citing Richardson*, 863 S.W.2d at 881*; Anglim v. Missouri Pacific Railroad Co.*, 832 S.W.2d 298, 303 (Mo. banc*), cert. denied Missouri Pacific R. Co. v. Anglim*, 506 U.S. 104 (1992).

[12] *Psychiatric Healthcare Corporation of Missouri v. Dep't of Social Services*, 100 S.W.3d 891, 900 (Mo. App. W.D. 2003), *quoting Jones v. City of Jennings*, 595 S.W.2d 1, 3 (Mo. App. E.D.1979).

[13] *State ex rel. Missouri Gas Energy v. Pub. Serv. Comm'n*, 186 S.W.3d 376, 382 (Mo. App. W.D. 2005).

Commission if the evidence permits either of two opposite findings.[14] A party challenging the Commission's decision bears the burden of proof to "show by clear and satisfactory evidence" that the Commission determination complained of is "unreasonable or unlawful." [15]

II. The Specific Allegations of Error

The remainder of this response will be organized generally according to the separate points raised by Noranda (which raised far more issues than the other parties), and will combine a response to points that Noranda had in common with OPC and AARP, where appropriate.

A. Noranda's focus on economic challenges in the country does not lawfully justify rehearing.

As discussed earlier, the Commission's job is to set just and reasonable rates based upon cost of service ratemaking principles which ultimately provide a reasonable opportunity for the utility to earn a fair ROE, with the utility to have the corollary obligation to serve all within its territory and to provide them with safe and adequate service. Noranda, without the support of any legal principle whatsoever, suggests that granting a justified rate increase to a utility "disregard[s]" the welfare of the state and that it is thus "unjust, unreasonable and otherwise unlawful."[16]

Noranda attempts to underpin this novel theory of ratemaking on the allegation that AmerenUE "by its own admission" failed to exercise proper cost control, citing two data request responses which outlined capital expenditures being reconsidered at AmerenUE given the liquidity crisis gripping the credit markets. AmerenUE has admitted no such thing. Indeed, there is not one shred of evidence in the record that the expenditures upon which the revenue

[14] *Id*.
[15] Section 386.430, RSMo. (2000).
[16] Noranda Rehearing Application, ¶ 1. The first four numbered paragraphs of Noranda's Rehearing Application are essentially a plea to the Commission to disregard its statutory and constitutional duty to set just and reasonable rates based upon cost of service ratemaking principles, and the evidentiary record, in view of the current economic difficulties. As noted earlier, addressing those economic policy or social issues is not the province of the Commission, but must be left to the market and the Legislature.

requirement set in this case is based were imprudently incurred or that legitimate, prudently incurred expenditures during the time when rates set in this case will be in effect will be lower than reflected in the historic test year in this case. That being the case, the Commission must give heed to those expenditures in setting the Company's rates.[17]

The data request responses cited by Noranda (Exs. 759 and 760) in fact show that AmerenUE was attempting to identify ways that it could cut expenditures in 2009 to preserve cash, given the liquidity problems it is facing. The record reflects that AmerenUE has looked across the board at how it might cut expenses, but that its costs will still be higher in 2009 than in the test year.[18] That a specific decision to cut 2009 capital expenditures had not been made in late November 2008, and that cost cuts for 2010 had not been examined as of that time, does not mean that a single dime of expenditures upon which rates set in this case are based was imprudent or improper, or that the rates reflected in the Report and Order are anything but just and reasonable

Noranda next claims that it was "mislead," apparently because it has not seen an immediate drop in borrowing costs or the cost of equity at AmerenUE (even though the rate increase has not yet even taken effect). Did Noranda's experienced counsel and consultant think that granting an FAC to AmerenUE would immediately reverse the spread between treasury yields and utility bond rates, or would instantaneously lower the cost of equity capital for AmerenUE?[19] While only they know what they thought, what is clear is that the Commission's

[17] *West Ohio Gas Co.*, 294 U.S. at 71. None of the contested issues resolved by the Commission in the Report and Order involved a claim by any party that the disputed item was imprudently incurred. Instead, any disputes regarding expenditures arose from things like a claim that an item was non-recurring (e.g., MISO Day 2 charges) or that there was a lack of proof (e.g., capital structure).

[18] Tr. p. 189, l. 17 to p. 191, l. 14.

[19] What "increased" cost of borrowing is Noranda talking about? The rates set in this case are based upon AmerenUE's actual capital structure and its actual weighted average cost of debt in the historic, trued-up test year. Does the record show that over time the timely recovery of fuel costs will improve AmerenUE's credit metrics and financial performance in a way that should lower the cost of borrowings versus what the cost of those borrowings

decision in this case is supported by the record. That is, the record established that AmerenUE's credit rating had already been downgraded at least in part due to the prior lack of an FAC, and that AmerenUE's credit rating may be upgraded (or avoid further downgrades) in the future once an FAC is implemented. The record also established that since just about every other electric utility in the country operates with an FAC, use of those electric utilities in the ROE experts' proxy groups necessarily means that granting AmerenUE an FAC does not dictate a cut in their recommended ROEs. Some of the ROE witnesses argued otherwise, but the Commission was free to judge their credibility, and the facts in the record, and to instead agree with Dr. Morin (and common sense) in finding that lack of an FAC would have justified an even higher ROE. The record in this case shows that without an FAC, AmerenUE might for that reason suffer further debt downgrades which would raise its borrowing costs.[20]

Noranda's next attempt to characterize the record in this case in a manner that would convince the Commission to depart from its duty to set cost-based rates is to argue that "the bulk of the evidence used by AmerenUE to support its request for a fuel adjustment clause was a forward-looking view of a world with ever increasing costs."[21] That statement is false. AmerenUE presented un-refuted evidence of its *historical* under-recovery of $114 million of coal costs alone from January 1, 2007 through March 1, 2009 (only a small part of which related to the period post-September 30, 2008, the trued-up test year cutoff date). Moreover, to the extent AmerenUE pointed to higher future fuel costs, a great bulk of those higher costs (as FAC opponents repeatedly pointed out) were hedged at varying percentages over the next five years.

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would be without those timely cash flows? Absolutely. Does that mean that AmerenUE's revenue requirement today is instantaneously lower than in the trued-up historic test year ? No.

[20] Noranda advances a variation of this theme later in its rehearing application, arguing that the Commission arbitrarily increased AmerenUE's ROE based upon AmerenUE's lower bond rating versus the bond rating of Mr. Gorman's proxy group based upon Noranda claim that an FAC will raise AmerenUE's bond rating.

[21] Noranda Rehearing Application, ¶ 3.

Noranda's point is, apparently, that the country is in a recession so fuel costs may not go up. But Noranda ignores the huge under-recoveries – the historic under-recoveries – AmerenUE has experienced, ignores the hedged (i.e., locked-in) fuel cost increases AmerenUE is facing, and ignores that lower recessionary prices will (and have, as the record reflects) also lower off-system sales prices, and will thus lower revenues at AmerenUE. And Noranda ignores that while AmerenUE has hedged some fuel costs for up to five years into the future, it could not similarly hedge off-system sales at the higher prices observed last Summer, meaning AmerenUE will face higher fuel costs but may in fact face lower off-system sales. Consequently, the recession Noranda spends so much time talking about may in fact increase, not decrease, AmerenUE's revenue requirement. Moreover, there are limits on what AmerenUE can do to respond to a recession given that it is obligated to spend the dollars necessary to provide safe and adequate service; must spend the dollars necessary to comply with the Commission's new reliability-related rules; and must continue to invest in its system (to meet the aforementioned obligations over the long term).[22]

B. The total rate increase is supported by the record.

Paragraph 5 of Noranda's rehearing application claims that the "overall level of rate increase" is not supported by the record. Focusing upon the Staff's and the Company's (the only parties who performed revenue requirement studies) revenue requirement evidence demonstrates that Noranda's statement is simply not true. There was ample evidence of record to support a

[22] Noranda unjustifiably criticizes the Commission when it claims that the Report and Order "[u]ncomfortably" creates the appearance that the Commission did not discharge its duty in this case, and also falsely suggests that AmerenUE had something to do with Noranda's loss of power on or about January 28. Noranda's Rehearing Application, ¶ 3. With respect to the latter charge, we would again point the Commission to the record in Case No. EA-2005-0180, which demonstrates, by Noranda's own testimony, that its plant is served by the lines of Associated Electric Cooperative, Inc. (AECI) (although given the 4-plus inches of ice that fell on Southeast Missouri, AmerenUE does not suggest fault on AECI's part). As to the former point, the record supports the Commission's decision to set rates based upon AmerenUE's legitimate trued-up test year level of expenditures, its actual capital structure, and with an allowed ROE well within the range of ROE's supported by the record.

nearly $190 million rate increase[23] (after taking into account all issues that were settled/resolved by the time the evidentiary hearings closed). The Commission awarded a revenue requirement increase of approximately $30 million less than that. Noranda's disagreement with how the Commission resolved certain contested issues does not erase the evidence of record that supports the Commission's decision. Indeed, Noranda does not claim that the Commission mis-valued any of the contested issues that it resolved in the Company's favor.[24]

C. The Commission's adoption of AmerenUE's actual capital structure was not error.

Noranda and OPC both claim error[25] in the Commission's use of AmerenUE's actual capital structure as of the end of the test year. They both characterize the issue as one involving the "burden of proof."

At the evidentiary hearing, Commissioner Jarrett asked Mr. O'Bryan the following, direct questions, to which the following direct answers were given:

> Q. Just one quick question. I just wanted to make sure that I'm understanding this correctly. You are proposing AmerenUE's actual capital structure as of December 31st, 2007?
> A. It was updated in my supplemental direct to March 31st, 2008.
> Q. But you're proposing that [sic] the actual capital structure?
> A. Yes.[26]

The Commission is free to believe Mr. O'Bryan, and to either disbelieve Mr. Hill or to find that Mr. Hill did not disprove Mr. O'Bryan's direct statement; that is, that the actual capital structure as of the end of the test year (March 31, 2008) was used. There was no shifting of the burden of proof. To the contrary, the Commission simply believed Mr. O'Bryan. Thus,

[23] *See* Staff's True-up Reconciliation and the Ex. 81 (True-Up Direct Testimony of AmerenUE Witness Gary S. Weiss).
[24] At bottom, Noranda simply has a "disagreement . . . over the amount that should be included in the [ratemaking] formula." Report and Order, p. 11.
[25] Noranda Rehearing Application, ¶ 6; OPC Rehearing Application ¶ 2.
[26] Tr. p. 596, l. 6-14.

AmerenUE sustained its burden, and the Commission's decision on this issue is supported by substantial and competent evidence of record.

Not only did Mr. O'Bryan provide competent evidence on this issue at the evidentiary hearing, but his rebuttal testimony also supports the Commission's conclusion. That testimony provides in pertinent part as follows:

> **Q. Why was it incorrect to make such an adjustment to AmerenUE's common equity in this case?**
>
> A. AmerenUE's total UES balance *prior to the end of the first quarter of 2008* contained the undistributed earnings of its wholly-owned unregulated subsidiaries. As I stated in my supplemental direct testimony these subsidiaries are no longer owned by AmerenUE (emphasis added).[27]

Because the balance contained these earnings *prior* to the end of the first quarter of 2008 (prior to March 31, 2008), the balance could not have contained those earnings as of the end of the test year, meaning that the capital structure presented in Mr. O'Bryan's supplemental direct testimony (which incorrectly used balances as if the balances did include those earnings) was necessarily wrong and did not reflect the actual capital structure for AmerenUE, upon which rates were ultimately set.

D. An ROE reduction in light of the FAC is not appropriate.

Noranda and OPC both[28] re-argue the points already made in their post-hearing briefs[29]; that is, their contention that AmerenUE's ROE should be reduced below the various experts' recommendations if an FAC is granted. As previously discussed, they are obviously incorrect about this point, since almost every other integrated electric utility in the country already benefits from the use of an FAC.

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[27] Ex. 8 (O'Bryan Rebuttal), p. 8, l. 7-12.
[28] Noranda Rehearing Application, ¶ 7; OPC Rehearing Application ¶ 6. AARP also raises the same argument in its rehearing application.
[29] Noranda Post-Hearing Brief, pp. 28-29; OPC Post-Hearing Brief p. 8.

The Commission aptly and convincingly disposed of this argument based upon evidence of record at pages 28-30 of the Report and Order. This point is nothing but an attempt to re-litigate a decided issue, without any legitimate allegation of error or changed circumstances that would justify rehearing.

E. The increased risk associated with integrated utilities was established by the record in this case.

Noranda claims, incorrectly, that there is no substantial and competent evidence of record supporting the greater risk faced by an integrated electric utility operating several large generating units, including a nuclear plant. Dr. Morin specifically testified to the higher allowed returns for integrated versus non-integrated (i.e., "wires only") utilities, and to the fact that wires only utilities are less risky.[30] The Commission was free to believe Dr. Morin's testimony on this point, and its finding that wires only utilities are less risky is indeed supported by the record.

E. The evidentiary record supports the Commission's examination of the ROE recommendations in this case, including Mr. Gorman's recommendation, in light of the results of constant-growth DCF analysis.

Noranda claims error in the Commission's criticism of Mr. Gorman for ignoring his own constant-growth DCF analysis results in arriving at his ROE recommendation.[31] Noranda's principal basis for its criticism arises from its claim that the Commission did not find it necessary to include constant-growth DCF analysis results in some recent Commission cases. The irony of this criticism is striking, given that just two paragraphs later, in ¶¶ 11 and 12 of its rehearing application, Noranda criticizes the Commission for considering other rate case decisions in arriving at its decision on two different issues in this case. Which is it – are Commission actions in other cases pertinent to this case, or aren't they?

[30] Ex. 4 (Morin Rebuttal) p. 5, l. 7 to p. 6, l. 6; Tr. p. 405, l. 6 to p. 406, l. 2.
[31] Noranda Rehearing Application, ¶ 9.

Regardless, the record in this case contains strong support for including consideration of Mr. Gorman's constant-growth DCF analysis results in evaluating his ROE recommendation, as explained in detail at pages 17 – 19 of AmerenUE's Post-Hearing Brief. Indeed, Dr. Morin's testimony provides specific evidentiary support for the Commission's criticism of Mr. Gorman's discard of his constant-growth DCF results.[32] The Commission's rationale for its concern with Mr. Gorman's complete disregard of his constant-growth DCF analysis results in light of the record in this case could not be more clear:

> The Commission will not attempt to recalculate Gorman's two-stage and multi-stage DCF models using different inputs, but the problems with those models illustrate the desirability of considering his model that produces a relatively high return on equity as a balance to his DCF models that show a relatively low return on equity. In that way, the possibly unreasonable impact of one model is counterbalanced by other models. There simply is no good reason to ignore the results of Gorman's constant-growth DCF.[33]

Noranda also criticizes the Commission by suggesting that the Commission simply discarded any analysis that suggested a lower ROE. That criticism is unfair, misleading, and misstates the Commission's decision. In evaluating Mr. Gorman's recommendation, the Commission did not discard any of the methods he used that produced lower results – in fact, both of his sub-10% ROE analyses (two-stage growth DCF and multi-stage growth DCF) were considered and their effect on the overall average of Mr. Gorman's analyses was included to reach the starting point used by the Commission to consider what it believed would be a more appropriate result if other flaws in Mr. Gorman's analysis were taken into account.[34]

[32] Ex. 4 (Morin Rebuttal) pp. 37-42.
[33] Report and Order, p. 22.
[34] Had those analyses been "discarded" the starting point would have become 10.96%, not 10.51%.

G. As explained by the Court of Appeals for the Western District of Missouri in its recently-issued opinion relating to AmerenUE's last rate case,[35] the Commission is not required to accept "a" recommendation from any particular ROE witness.

In the appeal of AmerenUE's last rate case, both Public Counsel and the State (the parties appealing the Commission's ROE decision) claimed the Commission erred in using Mr. Gorman's overall recommendation of 9.8% as a "starting point" while ultimately awarding an ROE that was not specifically recommended by any ROE expert (10.2%). Noranda essentially makes the same argument now, criticizing the Commission for varying from Mr. Gorman's base recommendation of 10.2%.[36] As the Western District Court of Appeals stated, "[t]he Commission was not obligated to believe all of Gorman's testimony . . .." Indeed, in the ROE decision just upheld by the Western District, the Commission examined the various experts' recommendations and analysis, found problems with various parts of various experts' recommendations, and ultimately reached a conclusion that was within the range of the evidence supported by the various recommendations. The Commission did the same thing in this case. This is proper, as the Western District's opinion demonstrates.

On a related point, OPC's criticism of the Commission's determination that Mr. Hill's recommendation was not credible misses the mark as well.[37] Contrary to OPC's claim, the Commission did not find that Mr. Hill's recommendation was not credible "entirely" because his recommendation was an outlier. Rather, the Commission noted that Mr. Hill generally testifies on behalf of consumer advocates (a perhaps surprising fact, given Staff's supposed role as an objective party), and notes that Mr. Hill's recommendation was more than 100 basis points beyond the average allowed ROE in the country – which puts him outside the zone of

[35] *State ex rel. Public Counsel et al. v Pub. Serv. Comm'n*, Case No. 69259 (W.D. Mo. January 13, 2009).
[36] Noranda Rehearing Application, ¶ 10 (Alleging that it is "arbitrary and capricious to selectively adopt pieces and parts [of] return on equity witnesses' testimony while accepting none of the unified recommendations.").
[37] OPC Rehearing Application, ¶ 5.

reasonableness the Commission has used for the past several years. These facts, among many, support the Commission's evaluation of Mr. Hill's recommendation.

H. Noranda and OPC's claim that there is no evidentiary support for the Commission's belief that Mr. Gorman's base recommendation is too low in failing to take into account the difference in bond ratings between AmerenUE and Mr. Gorman's proxy group and in failing to account for the quarterly payment of dividends misstates the record.

Both Noranda and OPC claim that the Commission based its decision in this case on its decision in the last rate case involving The Empire District Electric Company. From that basic argument they claim the record in this case does not support the Commission's criticism of Mr. Gorman's base recommendation, as outlined generally at pages 22 to 24 of the Report and Order.[38]

The first claim of error deals with the Commission's belief that Mr. Gorman's base recommendation was too low by approximately 20 basis points for failing to take into account the difference in bond ratings between AmerenUE and Mr. Gorman's proxy group. The record *in this case* reflects that there is a correlation between the quality of a utility's bonds (i.e., its bond rating) and allowed ROEs.[39] In fact, Dr. Morin specifically testified *in this case* that a 25 basis point adjustment, like that made in the *Empire* case referred to above, would be appropriate in *this case*.[40] Indeed, Mr. Gorman himself admits that the risk of a lower rated company is greater than of a higher rated company.[41] It is undisputed that Mr. Gorman's proxy group has an

[38] Noranda Rehearing Application, ¶¶ 11-12; 15 ; OPC Rehearing Application ¶¶ 3-4. As noted earlier, it's ironic that Noranda complains of the Commission's consideration of its prior decision in the *Empire* case, when Noranda itself complained (in its rehearing application at ¶ 9) that the Commission failed to consider its prior decisions.
[39] Tr. p. 412, l. 10-19.
[40] Tr. p. 463, l. 21 to p. 464, l. 18.
[41] Tr. p. 574, l. 20 to p. 576, l. 7.

average bond rating of BBB+ versus AmerenUE's BBB-.[42] In short, the record in this case provides direct support for the Commission's decision to make this adjustment.[43]

The second claim of error deals with the Commission's belief that Mr. Gorman's base recommendation was too low by approximately 20 basis points because of Mr. Gorman's failure to recognize that dividends are paid quarterly, not annually. Oddly OPC, while admitting that there is evidence of record in this case that would support a 20 basis points adjustment,[44] then complains about a much lower 5 basis point adjustment that leads to a lower ROE. Noranda does not claim error in the Commission's much lower adjustment than the record would have supported, but argues that the Commission looked to a different case (and not the record in this case) to make this adjustment.

Ignoring Mr. Hill's recommendation, the ROE recommendations in this case, with an FAC, ranged from approximately 10% to 10.9%. With respect to the quarterly versus annual DCF issue, the evidence *in this case* would have supported a 20 basis point adjustment to Mr. Gorman's analysis. The Commission very conservatively made only a 5 basis point adjustment, and awarded an ROE within the range of the evidence presented in this case. The Commission did not err.

I. Noranda's claim that the UCCM decision prohibits fuel adjustment clauses even though FACs are now specifically authorized by statute fails; indeed, the courts have already ruled against this very argument.[45]

In *State ex rel. Utility Consumers Council of Missouri v. Pub. Serv. Comm'n*, 585 S.W.2d 41 (Mo. 1979) (the UCCM case), the Missouri Supreme Court invalidated FACs then being used

[42] Ex. 600 (Gorman Direct) Sch. MPG-3, pp. 1-3.
[43] OPC mistakingly alleges that there is no evidence that 25 basis "is a valid starting point." OPC Rehearing Application ¶ 3. In fact, there is. Tr. p. 463, l. 21 to p. 464, l. 18 (a 25 basis point adjustment would be appropriate). Surely OPC can't be heard to complain that the Commission made a *smaller* 20 basis point adjustment when a 25 basis point adjustment was supported by the record.
[44] OPC Rehearing Application ¶ 4; Tr. p. 433, l. 16 to p. 435, p. 6.
[45] Noranda Rehearing Application, ¶¶ 13-14.

by electric utilities for residential customers in Missouri based upon a lack of statutory authority for such clauses in Chapters 386 and 393, RSMo. Judge Rendlin concurred in the majority opinion (decided 6-0), and invited the Legislature to address this lack of statutory authority "without undue delay." Judge Rendlin was joined in his concurrence by Judges Morgan and Donnelly. The basic holding of the UCCM case is that Section 393.140(11) and 393.150, RSMo. (2000) created a ratemaking process whereby rates could only be set (and changed) in a full-blown rate case, absent statutory authority to allow rate changes outside a rate case. Although the Legislature did not act to authorize such changes – such rate adjustment mechanisms – for another 16 years, in 2005, the Legislature provided the necessary statutory authority by enacting S.B. 179, which specifically authorizes rate adjustments outside general rate proceedings.

Despite this specific statutory authority to adjust rates outside a rate case, Noranda now argues that fuel adjustment clauses remain illegal under the *UCCM* decision. While Noranda states that its argument is based on Due Process grounds and declines to use the phrase "retroactive ratemaking," it is apparent that what Noranda is arguing is that an FAC, despite being authorized by S.B. 179, violates the prohibition against retroactive ratemaking, which is itself rooted in the Due Process clause. The flaw in Noranda's argument is that the Missouri Court of Appeals for the Western District of Missouri has *already rejected this argument.* [46]

As the Court explained in the MGUA case, the PGA (and the FAC here) are "applied only to future customers and future bills. The Companies are not allowed to adjust the amount charged to past customers either up or down."[47] In rejecting the argument Noranda makes now,

[46] This argument is essentially the same argument made by Mr. Conrad and OPC in the late 1990s in *State ex rel. Midwest Gas Users' Assn v. Pub. Serv. Comm'n*, 976 S.W.2d 470 (Mo. App. W.D. 1998) (the MGUA case), when Mr. Conrad's client, MGUA, attempted to invalidate the purchased gas adjustment on retroactive ratemaking grounds. Mr. Conrad's associate, Mr. Woodsmall, is also currently making the same argument in KCP&L Greater Missouri Operations Company's current FAC adjustment proceeding, Case No. EO-2009-0254.

[47] 976 S.W.2d at 481.

the Court concluded that "while they [the utilities] may consider past costs,[48] they thus apply only in the future and thus do not constitute retroactive ratemaking." *Id.*

J. Noranda and OPC re-argue the sharing percentage issue.

Noranda, OPC and AARP each complain that the sharing percentage adopted by the Commission in the FAC is too low.[49] All of their arguments were made during the litigation of this case, and this point is nothing but an attempt to re-litigate a decided issue.

The record is replete with support for the Commission's decision to adopt the 95%/5% sharing mechanism, as outlined and cited to at pages 66 to 71 of AmerenUE's Post-Hearing Brief and as also recounted at pages 70 to 76 of the Report and Order.

K. The FAC is reasonably designed to provide AmerenUE with a sufficient opportunity to earn a fair ROE.

While they do not come out and say so, Noranda and OPC's claim that the FAC gives AmerenUE an opportunity to earn more than a fair ROE[50] is essentially the same argument that was made in the FAC rulemaking proceedings; that is, that the FAC must include an "earnings test" that caps earnings whenever an FAC is in place. That argument has been rejected on multiple occasions by this Commission,[51] and it should be rejected again now.

The FAC no more gives AmerenUE an unlawful opportunity to earn more than its allowed return than might the possibility that abnormally hot weather could allow AmerenUE to

[48] In fact, the Commission's FAC rules mandate that only past costs be considered, although many jurisdictions use projected costs. Under Noranda's logic, were projected costs used (which would be allowable under S.B. 179), there would be no retroactive ratemaking. In any event, setting a future rate adjustment applied prospectively by using historic costs is not retroactive ratemaking, as the MGUA court concluded.
[49] Noranda Rehearing Application, ¶¶ 16-17; OPC Rehearing Application ¶ 9; AARP Rehearing Application, p. 2
[50] Noranda Rehearing Application, ¶ 19 ; OPC Rehearing Application ¶ 8. AARP makes a similar argument at page 2 of its rehearing application.
[51] The Company invites the Commission to take administrative notice of these arguments and its rejection of them in its FAC rulemaking docket, Case No. EX-2006-0472.

earn more than its allowed return in a given period.[52] Noranda and OPC argue that an FAC must somehow be designed to cap the return a utility can earn. Nothing in the statute so provides. Indeed, the statute provides that it must be *reasonably designed*; i.e., given the facts and circumstances under consideration in the rate case where the FAC is established, the Commission has to make a judgment that the FAC design is reasonable with respect to how it impacts the utility's opportunity to earn its allowed ROE.

Nor does Noranda's misleading and oversimplified calculation in paragraph 19 of its rehearing application support its novel argument. First, Noranda compares the average of 89 basis points of under-earnings at AmerenUE since June 2007 (which was only through March 31, 2008, and which under-earnings got worse as the case progressed) to AmerenUE's earlier, lower, allowed ROE from its last rate case (10.2%). Compared to its current cost of equity as determined by the Commission, that under-earning, assuming all else were equal (which it is not) would be nearly 150 basis points. Second, Noranda's "calculation" is misleading and is a gross oversimplification of the ratemaking formula, which must take into account rate base investments, planned and unplanned outages, extraordinary expenses, normalized revenues, load growth (or loss), etc. Given the investments AmerenUE must make in its system and rising fuel costs, among other things (like rising labor and pension and medical costs), the record provides no support for Noranda's made-up claim that the FAC will produce over-earnings at AmerenUE, particularly given that the FAC simply allows recovery of

[52] The prospect that AmerenUE would earn more than its allowed return, or that it can even reach its allowed return given its rising costs, locked-in fuel cost increases, and the fact that it will share 95% of any additional net fuel cost savings (e.g., if any savings could be generated by off-system sales), is unlikely in any event. This has become even more true given the current recession and its effect on AmerenUE's loads, and in view of the tens of millions of dollars of storm-related capital and operating and maintenance expenses AmerenUE is, at this moment, incurring to respond to the devastating ice storm in Southeast Missouri.

prudently incurred fuel and purchased power costs (offset by off-system sales revenues) – no more, and no less.

L. Allowing recovery of test-year vegetation management and infrastructure inspection costs caused by the Commission's new rules through a 3-year amortization is not retroactive ratemaking.

Noranda argues[53] that including test year expenditures above those included in rates set in the last rate case for vegetation management and for infrastructure inspection constitutes retroactive ratemaking. The additional expenditures at issue not only occurred in the test year, but they impact the revenue requirement established *in this case* upon which new rates, *prospectively*, will be based starting March 1, 2009. These expenditures do not result in the Commission changing any rate that was previously established (in Case No. ER-2007-0002, or otherwise), and thus cannot constitute retroactive ratemaking. Indeed, the Courts have been clear in holding that the Commission can consider past costs when setting rates that will only apply in the future.[54]

M. Allowing accounting authority for and deferral of vegetation management and infrastructure inspection costs post-September 30, 2008, and establishing a tracker for such costs, does not constitute retroactive ratemaking.

Noranda and OPC also argue that the deferral of expenditures from September 30, 2008 to March 1, 2009 and the prospective tracking of these expenditures constitutes impermissible retroactive ratemaking.[55] OPC made a similar argument regarding the SO_2 Tracker established in the Company's last rate case. The Commission properly rejected that argument, citing the

[53] Noranda Rehearing Application, ¶¶ 20-21. Although less clear because OPC mixes and matches different concepts and arguments in one point, OPC also apparently makes the same argument. *See* OPC Rehearing Application ¶ 7.
[54] *See, e.g., MGUA*, 976 S.W.2d at 481; *State ex rel. Missouri Gas Energy v. Pub. Serv. Comm'n*, 210 S.W.3d 330, 335-36 (Mo. App. W.D. 2006); *Report and Order*, Case No. ER-2007-0002, pp. 76-77 (citing *Missouri Gas Energy*).
[55] Noranda Rehearing Application, ¶¶ 22-24 ; OPC Rehearing Application ¶ 7.

Missouri Gas Energy case, *supra*.[56] For the same reasons, Noranda's and OPC's arguments fail here.

N. Allowing recovery of ice storm expenses deferred in an accounting authority order does not constitute retroactive ratemaking.

Noranda, ignoring years of Commission practice and ignoring cases such as *MGUA* and *Missouri Gas Energy*, *supra*, also argues that the Commission engaged in unlawful retroactive ratemaking when it included an amortization of the January 2007 ice storm expenses that had been deferred via accounting authorization previously granted by the Commission in the revenue requirement in this case.[57] To repeat, the courts have held that the Commission is free to consider past expenditures in setting rates *prospectively*. The courts and the Commission have, for decades, rejected the argument Noranda now makes. *See, e.g.*, *Re: Kansas City Power & Light Co*, Case No. EO-85-185, 75 P.U.R 4th 1 (Apr. 23, 1986). The Commission has simply done what it has for decades been authorized to do– allow the recovery of extraordinary ice storm costs through rates set prospectively.

O. Allowing recovery of MISO Day 2 expenses does not constitute retroactive ratemaking.

Noranda, this time alone, claims that allowing recovery of the MISO Day 2 expenses paid by AmerenUE during the test year due solely to a mistake by the MISO also constitutes retroactive ratemaking. AmerenUE paid these expenses in the test year. These costs affect the revenue requirement *in this case*, and impact rates *prospectively*. Consequently, there is no retroactive ratemaking.

[56] *Report and Order*, Case No. ER-2007-0002, pp. 76-77.
[57] Noranda Rehearing Application, ¶ 25.

P. Declining to adopt OPC's isolated depreciation rate adjustment for just five plant accounts in the absence of a comprehensive depreciation study was proper.

Noranda and OPC, without citation to any authority claims error on the Commission's part in not adopting OPC's proposed, isolated depreciation rate adjustments relating to five Callaway Plant accounts.[58] Noranda claims failure to make these adjustments "significantly overcompensates" AmerenUE. OPC claims that it is "rank speculation" that a depreciation study may show other changes that would offset OPC's proposed adjustment.

It is OPC who engages in "rank speculation." A depreciation study, as the Commission recognized in the Report and Order, is a complex, comprehensive look at a myriad of factors that inform the Commission's ability to set appropriate depreciation rates. Without a current study, making any change to depreciation rates is speculative. OPC's claim that its isolated adjustments would not be offset by other changes, and Noranda's claim of a "significant overcompensation" are themselves speculative. Depreciation rates were set in the last rate case based upon a comprehensive depreciation study and a consideration of all facts and circumstances. OPC proposed to change those rates in this case. Consequently, it was OPC's burden to convince the Commission that its proposed changes were appropriate, which it failed to so, and which indeed it should not be allowed to do absent a comprehensive study.

OPC claims its adjustment of selected depreciation rates is justified by a significant change in circumstances that has occurred since the last rate case—AmerenUE's announcement that it will pursue a license extension for the Callaway Plant. But as the Commission has recognized, this represents no significant change at all. In the last rate case the Commission assumed that the Callaway Plant's life would be extended. The Commission did not err in rejecting OPC's attempts to selectively lower depreciation rates for the nuclear plant accounts.

[58] Noranda Rehearing Application, ¶ 27; OPC Rehearing Application ¶ 10.

Q. A separate concurring opinion by a Commissioner who concurs in the Report and Order in all respects does not violate Missouri law.

Noranda's claims that "Missouri law" prohibits a Commissioner[59] from filing a concurring opinion that provides an analogy relating to the majority opinion issued in this case. Not surprisingly, Noranda's claim of what "Missouri law" requires is unsupported by citation to any statute, case or other rule of law.

What Missouri law "requires" is that a majority of a quorum of the Commissioners concur in decisions of the Commission.[60] It is undisputed that this occurred: three of the five sitting Commissioners voted for the Report and Order and all three concurred in that decision. Indeed, the Minutes of the Agenda meeting where the Report and Order was adopted reflect that three Commissioners unconditionally voted for the Report and Order, and Commissioner Davis' concurring opinion states that he "concur[s] with the majority opinion *in all respects*" (emphasis added).

R. AARP asserts no bases whatsoever that justify rehearing of its hot weather safety program issue.

AARP's rehearing application, which in fact appears to be a motion for reconsideration, simply re-litigates a decided issue without offering any reasons whatsoever that indicate any error in the Commission's original decision or any changed circumstance that would justify rehearing. AARP proposed this program, changed it in midstream, and failed to prove any

[59] Noranda Rehearing Application, ¶ 26. Since the only concurring opinion that was issued was issued by Commissioner Davis, it is apparent that Commissioner Davis' slightly more than one page concurring opinion is the subject of Noranda's argument.

[60] Section 386.130, RSMo. (2000), *discussed in State ex rel. Philipp Transit Lines, Inc. v. Pub. Serv. Comm'n*, 552 S.W.2d 696 (Mo. banc 1977). Perhaps Noranda intends to rely upon *State ex rel. St. Louis County v. Pub. Serv. Comm'n*, 228 S.W.2d 1 (Mo. 1950), wherein a reversal of a Commission Report and Order was upheld when a third Commissioner, who only concurred in *the result* of the original Report and Order (joined in by just two of five Commissioners), did not do so until 13 days later and indeed did not do so until the day before Applications for Rehearing were due. Under those circumstances, the Report and Order was unlawful because it was supplemented so near the effective date. *Id.* at 273. Consequently, *St. Louis County* provides no support for Noranda's argument, given that the Report and Order in this case was concurred in in all respects by three of five Commissioners, and the Report and Order was issued 10 days before it was effective.

evidence that it was likely to work. As pointed out in AmerenUE's Post Hearing Brief, there also exists a legitimate concern about whether the Commission (as opposed to the Legislature) should be in the business of effectively taxing ratepayers to fund social programs, like the proposed hot weather bill credit. Rehearing (or reconsideration) of this issue is simply not warranted.

III. Noranda's Motion For Stay

At this moment, the record establishes that AmerenUE does not have a sufficient opportunity to earn a fair ROE and that just and reasonable rates cannot possibly be in place post-March 1, 2009 without implementation of the rate increase authorized in the Report and Order.[61] Given Noranda's failure to present any justification for rehearing of the Report and Order, it is incumbent on the Commission to allow that rate increase to take effect, as discussed in some detail in Section I of this Response.

While the cases provide minimal guidance, it is generally accepted that there are four considerations the Commission must apply in evaluating a request for a stay:

> [T]he determination of whether a stay [should be granted]. . . must be based on a balancing of four factors. These factors are: (1) the likelihood that the party seeking the stay will prevail on the merits of the appeal; (2) the likelihood that the moving party will be irreparably harmed absent a stay; (3) the prospect that others will be harmed if the court grants the stay;and (4) the public interest in granting the stay.[62]

As outlined above, there is little likelihood Noranda will prevail on any appeal, clearly AmerenUE will suffer great harm if a stay were granted by continuing itself to fail to earn a fair

[61] Granting AmerenUE's Application for Rehearing and relief that will keep AmerenUE whole from the lost Noranda revenues (but no more), in order to preserve nearly one-half of the required rate increase, is also necessary if the rates set are to provide AmerenUE the constitutionally required opportunity to earn a fair return. If AmerenUE's Application for Rehearing is not granted, customers will unfairly and improperly receive double credit for revenues derived from the same power—once through jurisdictional revenues imputed to Noranda (which will not be received by AmerenUE) and a second time when AmerenUE sells the same MWh off-system and credits customers through the FAC. This double crediting is clearly unwarranted and should be corrected.

[62] *Ohio ex rel. Celebreeze v. Nuclear Regulatory Commn*, 812 F.2d 288 (6th Cir 1987), *citing Cuomo v. United States Nuclear Regulatory Commission*, 772 F.2d 972, 974 (D.C.Cir.1985).

ROE by tens or hundreds of millions of dollars per year, and the public interest (and the law for that matter) does not support depriving the Company of the rate increase this Commission has already found to be necessary to establish just and reasonable rates. Thus, Noranda fails to meet three of the four standards cited above.

Moreover, Noranda cites economic loss, which does "not constitute irreparable harm, in and of itself."[63] Thus, Noranda's request for a stay fails on all four counts.

The ice storm that has impacted Noranda's production is extremely unfortunate.[64] Perhaps federal or state disaster aid may help Noranda mitigate these impacts to some extent, or Noranda may have insured itself against business interruption or casualty loss, or both, as many businesses do. In the interim if Noranda's production remains at current reduced levels, Noranda's electricity charges will be reduced by tens of millions of dollars over the coming months, as addressed in the Company's Application for Rehearing, which will reduce the cash needed by Noranda for its operations. Given Noranda's comments about current aluminum prices, it may be that the opportunity cost of this reduced production is far less than it might have been at a different time. All of these things are possible, but they do not figure into the ratemaking equation or this Commission's charge as a body that regulates public utilities and sets just and reasonable rates according to cost of service ratemaking principles consistent with the Commission's statutory duties and the terms of the United States and Missouri Constitutions.

For the foregoing reasons, the Commission should deny the Applications for Rehearing of Noranda, OPC and AARP, and Noranda's Motion for Stay.

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[63] *Ohio ex rel. Celebreeze, citing Wisconsin Gas Co. v. F.E.R.C.*, 758 F.2d 669, 674 (D.C.Cir.1985).

[64] Noranda implies that AmerenUE somehow contributed to its loss of production. As explained in Case No. EA-2008-0180, cited in the Company's Application for Rehearing, Noranda is supplied by lines owned by AECI, under a separate transportation agreement between Noranda and AECI. AmerenUE suggests no fault on AECI's part given the devastating amounts of ice that fell, but given Noranda's statements, it is necessary to clarify again that means by which Noranda receives electricity produced by AmerenUE.

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CERTIFICATE OF SERVICE

I hereby certify that the foregoing Application and Motion was served via e-mail, to the counsel of record for all parties to this case, as follows, on the 10th day of February, 2009.

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