

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

IN THE MATTER OF: THE APPLICATION OF BIG
RIVERS ELECTRIC CORPORATION FOR AN
ADJUSTMENT OF RATES

Case No. 2013-00199

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DIRECT TESTIMONY
OF
STEVE HENRY

ON BEHALF OF THE
KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.

October 2013

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RIVERS ELECTRIC CORPORATION FOR AN : Case No. 2013-00199
ADJUSTMENT OF RATES :

**DIRECT TESTIMONY OF STEVE HENRY
ON BEHALF OF DOMTAR PAPER COMPANY, LLC
AS A MEMBER OF KENTUCKY INDUSTRIAL UTILITY CUSTOMERS, INC.**

I. INTRODUCTION AND QUALIFICATIONS

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Q. Please state your name, occupation, and business address.

A. My name is Steve Henry. I am the General Manager of Domtar Paper Company, LLC (“Domtar”) Hawesville, Kentucky pulp and paper manufacturing facility. My business address is PO Box 130, Highway 1406, Hawesville, KY 42348.

Q. Please describe your educational and professional background.

A. I earned a Bachelors of Science in Electrical Engineering from Virginia Polytechnic Institute and State University (Virginia Tech). I earned a Masters in Business Administration from NOVA Southeastern University. In addition, I have completed graduate pulp and paper coursework at North Carolina State University.

I have been an active participant in the pulp and paper industry since 1991,

1 initially with Georgia-Pacific from 1991 to 1996. I have worked in a variety of
2 engineering, operations/maintenance, management, and corporate roles in my career. I
3 was Vice President – Mill Manager for Weyerhaeuser and International Paper’s facility in
4 Cedar Rapids, Iowa from 2007 to 2010. For International Paper, I was the Investment
5 Project Manager of Containerboard Asset Strategy from 2010 to 2011. I joined the
6 Domtar organization and became General Manager of their Hawesville facility in August
7 2011.

8
9 **Q. On whose behalf are you appearing in this proceeding?**

10 **A.** I am appearing on behalf of Domtar and Kentucky Industrial Utilities Customers, Inc.
11 (“KIUC”). Domtar is the largest manufacturer and marketer of uncoated freesheet paper
12 in North America and the second largest in the world based on production capacity.
13 Domtar is also a leading marketer and producer of a broad line of incontinence care
14 products marketed primarily under the Attends® brand name as well as baby diapers.
15 Domtar’s Hawesville Mill, located in Hancock County, employs 445 colleagues. The
16 mill is one of the largest and strongest economic providers for the region. We produce
17 fine printing and writing papers, along with market pulp. Our products are used in homes,
18 offices, businesses, and schools. In addition to traditional printing and writing papers,
19 you can find our products everywhere from fast food restaurant paper bags to tea bag
20 packets to labels to multi-part forms. Our annual production capacity is almost 600,000
21 tons of paper and 100,000 tons of hardwood market pulp. Domtar is a member of KIUC
22 and is served under the Large Industrial rate by Kenergy Corp. and Big Rivers Electric
23 Corporation (“Big Rivers”).

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Q. Would you please summarize your testimony?

A. Yes. My testimony focuses on the adverse impact of a 111% rate increase on Domtar's Hawesville, Kentucky mill, making the Hawesville mill's power rate the least favorable rate of Domtar's five major U.S. mills. This would significantly undermine the competitiveness of that mill both in relation to the other Domtar mills and in relation to outside competitors.

I also support the KIUC Formula Rate Plan and witness Baron's recommendation that Large Industrial customers should be granted access to market-based rates for at least a portion of their load. It is inequitable for the smelters to have access to market-based rates while Big Rivers' remaining customers are precluded from any of the benefits of those rates. If the Commission does not accept the proposal, then I recommend it amend the terms of the Rural Economic Reserve fund so both Rural and Large Industrial customers can benefit from the fund.

Finally, I criticize Big Rivers' proposal to secure replacement load in the future by providing discounted rates to new customers in its service territory. It would be unreasonable for Big Rivers to provide significant discounts to new customers while forcing its existing industrial customers to see their rates more than double due to the costs associated with the departure of the smelters.

Q. Have you testified in any other proceeding(s) before the Commission?

A. Yes. I testified in Big Rivers' last rate case, Case No. 2012-00535.

1 **Q. Please summarize your testimony from Big Rivers' last rate case.**

2 A. I testified that the North American uncoated freesheet paper market has been declining at
3 a rate of 4% per year. This decline has caused and will continue to cause closures in our
4 segment of the paper industry.

5 I also testified about Big Rivers' proposed rate increase and public
6 misunderstanding of the true level of that increase. For example, though Big Rivers
7 claimed that the proposed increase to the Large Industrial class would be 17.9%, Domtar
8 calculated that the "all-in" increase (including non-base rate components) to the
9 Hawesville mill would be approximately 32%.¹

10 I explained that because the actual bill impacts that customers in Big Rivers'
11 service territory will experience from its proposed "pancaked" rate increases were not
12 well known, Domtar, Aleris, and Kimberly Clark founded Fair Rates Kentucky, a
13 coalition of businesses and individual utility customers in Western Kentucky. Fair Rate
14 Kentucky's mission is to educate the public concerning Big Rivers' plan to recover 100%
15 of costs resulting from the smelters' departure from its remaining ratepayers.

16 In addition, I discussed specific impacts of Big Rivers' requested rate increases on
17 Domtar's Hawesville mill. I calculated the rate increase proposed in that case alone
18 would cause Domtar's regulated electricity costs to jump by about \$1.6 million per year.
19 I projected that the impacts of this rate case would be even worse for Domtar.

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¹ See Tab 59 Attachment to Application of Big Rivers, Case No. 2012-00535, page 8 of 8. This is due primarily to the fact that Big Rivers' filing causes changes in non-base rate components of Domtar's bill such as the Fuel Adjustment Clause and the Member Rate Stability Mechanism.

1 **Q. Have any notable events occurred in the uncoated freesheet paper market since**
2 **your previous testimony was filed?**

3 A. Yes. On September 11, 2013, one of our competitors, International Paper, announced
4 that it plans to close the largest uncoated freesheet paper mill in North America (located
5 in Courtland, Alabama) due to shrinking demand. This will displace 1,100 workers and
6 remove 950,000 tons per year of paper capacity.² According to the Alabama Forestry
7 Commission, the closure will result in 5,402 total projected job losses in the region and
8 income loss of \$337 million³. The Courtland mill is one of the lowest cost mills
9 operating in the United States according to Fisher International.

10 In addition to the Courtland mill closure, both Boise and Georgia Pacific (G-P)
11 are also reducing uncoated freesheet capacity. Boise shut two paper machines at its
12 International Falls, Minnesota mill at the end of September; 300 workers are losing their
13 job as a result. G-P plans to shut a paper machine at its mill in Crossett, Arkansas, in
14 November.

15 According to RISI, the shutdown of the seven paper machines will result in the
16 total loss of capacity of 1.16 million tons. This represents 9% of industry capacity in
17 North America and is equivalent to twice the capacity of Domtar-Hawesville. These
18 significant closures highlight my concern that keeping operating costs as low as possible
19 is critical in the declining uncoated freesheet paper market where demand is falling
20 290,000 tons to 380,000 tons per year.

² "International Paper to Close Alabama Mill," *Wall Street Journal* (September 17, 2013), available at <http://online.wsj.com/article/SB10001424127887323595004579068902452270572.html>.

³ "Economic Impacts of the Closure of the International Paper Mill in Courtland, Alabama." Alabama Forestry Commission, available at <http://www.forestry.alabama.gov/PDFs/EconomicImpactsOfTheClosureOfTheIPMil%20inCourtland.pdf>.

1 **Q. How does Big Rivers' proposal in this case impact your previous testimony?**

2 A. Big Rivers' proposal makes the concerns expressed in my previous testimony even more
3 pressing. The information filed in this case provides a fuller picture of the rate impacts of
4 Big Rivers' proposals than was available when my testimony was filed in Case No. 2012-
5 00535. We have now calculated the total "all-in" rate increase for Domtar resulting from
6 the Century and Alcan rate cases will be 111.8% as of July 2014 when the Economic
7 Reserve is projected to be exhausted.

8

9 **Q. What would be the consequences of a 111% spike in Hawesville's power bill from**
10 **Big Rivers?**

11 A. The proposed 111% rate increase would further erode the Hawesville mill's position
12 among Domtar's major U.S. mills, making Hawesville's regulated electric rates the
13 highest of all of those mills.

14

15 Prior to August 20, 2013, Hawesville had the most favorable regulated power rate
16 of any of Domtar's five major U.S. mills. As the Table below indicates, the proposed
17 111% increase would move Hawesville's power rates to the bottom of the list of
18 Domtar's major U.S. mills once the Reserve funds are exhausted.

Mill	State	Regulated Rate
Hawesville (8/19/2013)	Kentucky	\$ 33.05 / MWh
Hawesville (8/20/2013)	Kentucky	\$ 43.34 / MWh
Johnsonburg	Pennsylvania	\$ 46.48 / MWh
Ashdown	Arkansas	\$ 55.08 / MWh
Kingsport	Tennessee	\$ 57.50 / MWh
Marlboro	South Carolina	\$ 68.56 / MWh
Hawesville (8/1/2014)	Kentucky	\$ 69.99 / MWh

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1 This situation is further exacerbated when those Domtar mills with “buy all/sell
2 all” agreements are taken into account. When all of those agreements are considered,
3 Hawesville’s *net* power costs were already the 4th most expensive out of the 5 mills at
4 Big Rivers’ rates as of August 19, 2013. Consequently, if the proposed rate increases are
5 approved, the Hawesville mill will trail even farther behind the other Domtar U.S. mills
6 in terms of *net* power rates.

7
8 **Q. Why does it matter if the Hawesville mill’s power rate is less favorable than other
9 Domtar facilities?**

10 **A.** As I explained previously, in addition to competing with other paper manufacturers, our
11 Hawesville mill competes with other Domtar mills for production rights and for Domtar’s
12 limited capital resources, based upon the cost of finished product. These rate increases
13 jeopardize access to what should be Hawesville’s share of corporate capital funding for
14 projects needed to keep our manufacturing processes both modern and competitive.

15 Additionally, at the direction of Domtar’s senior management, our mill is faced
16 with taking market downtime from time to time. This is a temporary idling of selected
17 Domtar mills because our overall production capabilities have exceeded market demands.
18 In light of current market conditions, any increase in the cost of production at Hawesville
19 increases the likelihood that we may be asked to temporarily halt production. In like
20 manner, these increases jeopardize access to what should be Hawesville’s share of
21 corporate capital funding for projects needed to keep our manufacturing processes both
22 modern and competitive.

1 **Q. What happens if less capital is available to the Hawesville mill?**

2 A. Given the current market conditions, if Hawesville's access to capital is reduced and its
3 costs of production are raised as a result of Big Rivers' proposed rate increases, the
4 frequency and duration of idling requests at Hawesville may increase. This idling not
5 only jeopardizes Hawesville's economic position compared to other Domtar facilities. It
6 also has environmental implications.

7 For every two tons of production, our pulping process yields enough residual
8 biomass fuel to offset one megawatt-hour of "brown power" produced from a coal or
9 natural gas-fired facility. For example, in 2012, the Hawesville facility produced
10 renewable energy to offset more than 255,000 MWh of the region's brown power. This
11 was enough renewable energy to power 22,600 average US homes for a year. Increased
12 idling requests would reduce the amount of renewable energy produced by the
13 Hawesville mill.

14

15

16 **Q. What do you recommend that the Commission do in response to Big Rivers'**
17 **proposed rate increases?**

18 A. In addition to adopting the KIUC Formula Rate Plan, which KIUC witness Kollen
19 recommends and can discuss in greater detail, I think the Commission should adopt
20 KIUC witness Baron's recommendation to allow Large Industrial customers access to
21 market-based rates for at least a portion of their load. It is inequitable to allow the
22 smelters to access market-based rates while precluding other customers of Big Rivers

1 from receiving at least a portion of the benefits of those rates.⁴

2 My counsel has advised that granting Large Industrial customers access to
3 market-based rates is legal since we would still be buying power from the utility that has
4 the exclusive right to serve our plant, Kenergy. Also, market-based rates for Domtar
5 would not violate the terms of the all-requirements contract that Kenergy has with Big
6 Rivers since Kenergy would still be supplied by Big Rivers. Allowing Domtar to access
7 market-based rates would also help us better manage our costs and would keep the
8 Hawesville mill more competitive than it would otherwise be if Big Rivers proposed
9 increases are ultimately approved.

10 If the Commission does not allow Large Industrial customers to access market-
11 based rates for at least a portion of their load, at minimum, I think it is very important for
12 the Commission to amend the terms of the Rural Economic Reserve fund so that both
13 Rural and Large Industrial customers can benefit from that fund, as recommended by
14 KIUC witness Baron.

15 In my opinion, it would be unreasonable and discriminatory for certain business
16 customers to receive more protection from Big Rivers' rate increases just because they
17 are classified as "Rural" rather than as "Large Industrial" like Domtar. This is especially
18 true since the Commission itself created the Reserve funds. Since Big Rivers received
19 those funds by order of the Commission, my understanding is that the Commission has
20 the power to change the use of those funds to protect all of Big Rivers' customers from
21 the proposed rate increases.

22 In sum, Domtar should be treated on a non-discriminatory basis compared to the

⁴ Century is already receiving the benefits of market-based rates as a result of Case No. 2013-00221.

1 Smelters and be given market-based rates for all or at least a portion of its load. Absent
2 that, we should be treated on a non-discriminatory basis compared to the thousands of
3 business customers classified as “Rural” and be given equal protection under all of the
4 reserve accounts.

5
6 **Q. Are there any other aspects of Big Rivers’ proposal that you find inequitable?**

7 A. Yes. As I understand it, the projections that Big Rivers is using to support its case rely
8 heavily upon the assumption that it will secure hundreds of megawatts of replacement
9 load in the near future. One way that Big Rivers proposes to secure that replacement load
10 is to provide discounted rates to new customers in its service territory. I find it entirely
11 unreasonable for Big Rivers to provide discounts to new customers while forcing its
12 existing customers to undertake tremendous rate increases. Current non-smelter
13 customers should not be forced to take on 100% of the burden of the smelters’ departure
14 and receive no discount while speculative new customers would receive substantial
15 discounts on their power rates.

16
17 **Q. Do you wish to add anything else regarding Big Rivers’ rate requests?**

18 A. Yes. As I stated previously, the team at Domtar's Hawesville facility is working hard
19 every day to keep our facility competitive in a declining commodity market. In a
20 competitive global marketplace we cannot afford to pay for 100% of the costs incurred to
21 serve other customers while Big Rivers’ creditors recoup 100% of their investments.
22 Investors make investments assuming a degree of risk and without any expectation that
23 they will be insulated from such risk. Domtar and the other ratepayers of Big Rivers are

1 not guarantors for the loans taken out by Big Rivers.

2 On behalf of my 445 colleagues at our Hawesville facility, their families, and our
3 local community, I again ask that this Commission consider only actions that will keep
4 our electric rates fair, just and reasonable so we can continue to serve our customers,
5 community and stakeholders by continuing to provide a useful, cost-effective, and
6 environmentally-sustainable product at a reasonable price. Thank you for your time and
7 consideration.

8 **Q. Does this conclude your testimony?**

9 **A. Yes.**

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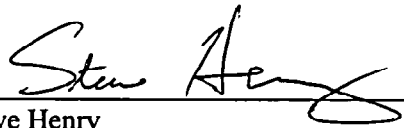
In The Matter Of: :
Application Of Big Rivers Electric Corporation For A : Case No. 2013-00199
General Adjustment In Rates :
:

AFFIDAVIT OF STEVE HENRY

STATE OF KENTUCKY)
COUNTY OF Hancock) SS


Steve Henry, being first duly sworn deposes and states that:

1. He is General Manager of Domtar Paper Company, LLC.
2. He is the witness who sponsors the accompanying testimony entitled "Direct Testimony of Steve Henry on behalf of Kentucky Industrial Utility Customers and Domtar Paper Company, LLC ";
3. Said testimony was prepared by him and under his direction and supervision;
4. If inquiries were made as to the facts in said testimony he would respond as therein set forth; and
5. The aforesaid testimony is true and correct to the best of his knowledge, information and belief.



Steve Henry

Subscribed and sworn to or affirmed before me this 24th day of October, 2013 by Steve Henry.



Notary Public

