Applicants' Ex. 36.0

ILLINOIS COMMERCE COMMISSION

DOCKET NO. 04-0294

SURREBUTTAL TESTIMONY

OF

JERRE E. BIRDSONG

Submitted On Behalf

Of

AMEREN CORPORATION

August 19, 2004

PUBLIC VERSION

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SURREBUTTAL TESTIMONY

OF

JERRE E. BIRDSONG

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

A. My name is Jerre E. Birdsong. I am Vice President – Risk Management and Treasurer of Ameren Corporation ("Ameren") and its operating subsidiaries. My business address is 1901 Chouteau Avenue, St. Louis, MO 63103.

Q. Are you the same Jerre E. Birdsong who previously submitted direct and rebuttal testimonies in this docket?

A. Yes, I am.

Q. What is the purpose of your surrebuttal testimony?

A. The purpose of my surrebuttal testimony is to respond to: Staff witness Sheena Kight regarding the modification of the dividend restriction to which Illinois Power Company ("IP") is now subject and the participation of IP as a lender in the Ameren utility money pool; Staff witness Michael McNally regarding the imputation of a debt redemption premium to certain bonds that IP intends to redeem; AG witness James Rothschild regarding IP's dividend policy, the post-acquisition capitalization of IP and the money pool; and IIEC witness Michael Gorman regarding IP's capital structure. I will also sponsor compromise positions regarding the dividend restriction and money pool issues.

Dividend Policy

Q. Ms. Kight questions your statement that IP will have access to $1.1 billion in liquidity after the transaction closes. Please respond.

A. Ameren Corp. currently has three syndicated credit agreements with a group of banks totaling $935 million. Ameren's utility subsidiaries, AmerenUE, AmerenCIPS, and AmerenCILCO, also currently maintain a total of about $229 million of bilateral credit facilities. The total of these facilities, just over $1.1 billion, would be available to IP as a participant in Ameren's utility money pool arrangement. The $935 million of facilities at the Ameren Corp. level would also be available to support direct loans by Ameren Corp. to IP.

Ameren is seeking approval for IP to have $500 million of short-term borrowing authority, an amount that Ameren believes is sufficient for IP to meet its short-term borrowing needs. My point in my rebuttal was simply that, in the extremely unlikely event that IP's short-term borrowing needs exceed the $500 million level, additional liquidity is available. Moreover, the Ameren Companies have four times the liquidity needed to support this borrowing level. Naturally, IP would need to seek regulatory approval to increase its short-term borrowing limit. The fact that Ameren has not sought approval for greater level of borrowing authority here indicates only that Ameren does not foresee a need for greater borrowing authority. It is still true, however, that Ameren's additional liquidity provides IP with additional assurance.

Q. Please respond to Ms. Kight's concern with IP paying dividends in violation of the provisions of Section 7-103 of the Public Utilities Act.

A. After the acquisition of IP by Ameren, Ameren commits that it will not allow IP to pay dividends in violation of any law or regulation, including the Public Utilities Act.

Q. Please comment on Ms. Kight's discussion of early redemption of the 11.5% bonds.

A. <**begin confidential** XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXX **end confidential>** Other than the equity claw back provision which allows for the redemption of up to 35% of the principal amount of these bonds at any time prior to December 15, 2005, the remaining outstanding portion of these bonds can be redeemed any time between December 15, 2006 and December 14, 2007 at a price of $105.75 per bond. **<begin confidential** XXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX

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Q. Have the Applicants reached an understanding with the Staff regarding the reinstatement of dividend payments by IP?

A. Yes. I have attached Applicants' Ex. ___.1, which is a dividend restriction to which Ameren will will agree. The Staff has also indicated that it does not object to this modified dividend restriction.

<u>Utility Money Pool</u>

Q. Please comment on Ms. Kight's alternative to IP lending to the Utility Money Pool.

A. Ms. Kight states at lines 119-121 of her rebuttal testimony that "on the few days on which IP has surplus cash, it can use the unilateral money pool instead of the Utility Money Pool to invest those surplus funds." I assume Ms. Kight is referring to the proposed "Unilateral Borrowing Agreement" between Ameren and IP. It is unilateral because IP can only borrow funds from Ameren under the agreement. The agreement we have filed (Applicants' Exhibit ____) is very clear and unambiguous in this respect. Section 1.1 of the agreement expressly provides that "Ameren may not borrow under this Agreement from AmerenIP." Also, by SEC rules, IP cannot loan funds to Ameren for it to invest. Therefore, Ms. Kight's alternative is not legally possible. Accordingly, if IP does not lend to the Utility Money Pool, Ameren Services will not be able to invest IP's surplus cash efficiently.

In Ms. Kight's footnote 16, she states that, "in its present form, the Utility Money Pool agreement would not permit IP to invest its surplus cash in the pool." This is not correct. She further states that "IP's surplus cash would first be used for lending before the funds would be considered for investing." Any surplus funds that IP loans to the pool and that in turn are borrowed by a sister utility represent IP's investment on which it will earn interest from the borrowing utility (at an internal borrowing rate which is higher than a lower, external short-term investing rate). This is the mechanism which prevents the negative carry and is the primary reason for managing liquidity through a pool rather than separately by affiliate. This also explains the source of the greater investment returns IP will be able to earn in the Utility Money Pool despite the investment limitations in 83 IL Adm. Code Section 340.50 addressed by Ms. Kight beginning at line 170 of her rebuttal testimony.

Q. Please address Mr. Rothschild's assertion that you have attempted to confuse his money pool testimony.

A. I have not misunderstood or misconstrued his testimony. The simple and undeniable truth of the matter is that IP cannot legally lend funds to Ameren, no matter what the source of the funds may be.

Q. Have the Applicants reached an understanding with the Staff regarding the participation of IP in Ameren's Utility Money Pool?

A. Yes. I have attached Applicants' Ex. ___.2, which is a statement of conditions to IP's participation in the Utility Money Pool to which Ameren would not object. Staff has indicated that it also does not object to this condition.

<u>Debt Redemption Premium</u>

Q. <begin confidential **XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX** end confidential>

A. **<begin confidential** XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX **end confidential>**

Ameren is willing to accept Mr. McNally’s estimate of $64.8 million for the debt redemption premium for the 11.5% bonds in spite of its obvious conservatism.

Q. Please comment on Mr. McNally’s conclusion that if the Commission accepts the alternative presented by IP in Docket No. 04-0476, then no call premium for the 11.5% would be recoverable since it never existed for ratemaking purposes.

A. This alternative was presented as a hypothetical situation “if the Commission determines that it would be inappropriate to include in the rate of return on rate base the full all-in cost of IP’s 11.5% bonds.” This hypothetical situation also results in the outstanding balance of the intercompany note being reduced by $550 million. This would result in an increase in IP’s equity balance by $550 million upon the closing of our proposed acquisition of IP when the note is eliminated. Therefore, the adoption of this hypothetical situation would require an increase in IP’s equity balance for ratemaking purposes of $550 million *ad infinitum*. Nevertheless, this hypothetical situation is not relevant to the issue at hand. The undeniable reality is that a sizeable premium must be paid to redeem the 11.5% bonds before IP can be returned to financial health under any recapitalization plan.

<u>Stock Issuance Costs</u>

Q. Does Ameren accept Mr. McNally's stock issuance cost calculation?

A. Yes. Ameren is willing to accept Mr. McNally’s stock issuance cost calculation of $22,387,950 in spite of its obvious conservatism.

Q. Please address Mr. Gorman’s contention that the equity issued by Ameren to finance the acquisition and recapitalization of IP benefits other Ameren affiliates because it protects the bond ratings of those companies.

A. As stated in my rebuttal testimony, all proceeds from the February and July equity issuances are being used to fund the acquisition or placed into IP to fund the recapitalization plan. My testimony is not in conflict with Mr. Baxter’s. When Mr. Baxter stated that the proposed capital structure protects existing bond ratings of other Ameren affiliates, he was referring to the fact that our recapitalization plan for IP **<begin confidential** XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX **end confidential>** (See Applicants’ Ex. 21.0, lines 50-82.) Yet, since the IP rating will still not be investment grade at all of the rating agencies, it cannot possibly be concluded that IP is being overcapitalized to assist other affiliates. Moreover, the simple fact is that, if

Ameren did not acquire and recapitalize IP, Ameren's affiliates' bond ratings would not need protection. The equity is required by IP solely for use at IP.

Capital Structure

Q. Please comment on Mr. Rothschild's conclusion that "for a regulated utility it is proper to focus on capital structure in reviewing bond ratings."

A. All rating agencies have indicated that, even for regulated utilities, capital structure is the metric to which they only give secondary emphasis from a quantitative standpoint in assigning ratings. The achievement or maintenance of a specific capital structure is in no way a guarantee that a specific rating will be assigned. Along with qualitative factors, cash flow metrics are given primary weight, and the capital structure is just the result of the impact of these more important factors. Mr. Rothschild's calculations ignore such real factors as non-balance sheet obligations and transitional funding notes, which have a significant negative impact on ratings.

Mr. Gorman's discussion of bond ratings suffers from the same deficiencies. The guidelines published by Standard & Poor's that Mr. Gorman references are merely that – guidelines. Meeting these specific guidelines is not a guarantee that a specific rating will be assigned. The June 1, 2004 research article wherein Standard & Poor's updated these guidelines stated:

> "It is important to emphasize that these metrics are only guidelines associated with expectations for various ratings levels. Although credit ratio analysis is an important part of the ratings process, [these statistics] are by no means the only critical financial measures that Standard & Poor's uses in its analytical process. We also analyze a wide array of financial ratios that do not have published guidelines for each rating category. Again, ratings analysis is not driven solely by these financial ratios, nor has it ever been. In fact, the new financial guidelines that Standard & Poor's is incorporating for the specific rating categories reinforce the analytical framework whereby other factors outweigh the achievement of otherwise acceptable financial ratios."

We have actual guidance from the rating agencies on IP's ratings – this guidance is IP-specific, and much more reasonable to rely upon than Standard & Poor's published guidelines. Also, Standard & Poor's published guidelines are specific to Standard & Poor's. Moody's would not use those or even recognize them for purposes of its assignment of ratings or the guidance they have provided to us.

Q. Please address Mr. Rothschild's discussions on the information you have received from Moody's concerning Ameren's proposed IP recapitalization plan.

A. When we provided Moody's with our recapitalization plan, including all the financial commitments that we made in Applicants' filing in this case, Moody's provided preliminary guidance that this recapitalized IP will receive a secured bond rating of no better than Ba1. Contrary to Mr. Rothschild's suppositions, this non-investment grade bond rating is based solely on financial parameters existing AFTER the proposed acquisition of IP by Ameren. The closing of the acquisition of IP by Ameren does not solve all of IP's financial woes. It will take time to reduce IP's indebtedness, and in fact, it could take up to two years before all of the 11.5% bonds are retired.

We know that Moody's provided preliminary guidance that Ameren's recapitalization plan results in a non-investment grade secured bond rating after its acquisition by Ameren. This requires no interpretation. The information was directly provided by Moody's. Moody's will not answer the question "What will it take to make it investment grade?" It will only provide ratings guidance for a detailed plan submitted to it.

Q. Does this conclude your surrebuttal testimony?

A. Yes, it does.