STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

CENTRAL ILLINOIS LIGHT COMPANY d/b/a AmerenCILCO, CENTRAL ILLINOIS PUBLIC SERVICE COMPANY d/b/a AmerenCIPS, and ILLINOIS POWER COMPANY d/b/a AmerenIP	)	
	)	**Docket Nos. 05-0160, 05-0161,**
Petitioners.	)	**05-0162 (consol.)**
	)	
Proposals to implement a competitive procurement process establishing Rider BGS, Rider BGS-L, Rider RTP, Rider RTP-L, Rider D, and Rider MV.	)	

INITIAL BRIEF OF THE STAFF OF THE ILLINOIS COMMERCE COMMISSION

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Staff of the Illinois Commerce Commission ("Staff"), by and through its counsel, pursuant to Section 200.800 of the Rules of Practice (83 Ill. Adm. Code 200.800) of the Illinois Commerce Commission's ("Commission"), respectfully submits its Initial Brief in the above-captioned matter.

I. EXECUTIVE SUMMARY

A. Introduction

On February 28, 2005, Central Illinois Light Company d/b/a AmerenCILCO ("AmerenCILCO"), Central Illinois Public Service Company d/b/a AmerenCIPS ("AmerenCIPS"), and Illinois Power Company d/b/a AmerenIP ("AmerenIP") (collectively, the "Ameren Companies", the "Ameren Utilities" or the "Companies"), simultaneously filed tariffs implementing a competitive procurement process. The Commission entered separate orders to suspend each of the tariffs and initiated

Dockets 05-0160, 05-0161, and 05-0162 on March 9, 2005. On April 8, 2005, the Commission granted the Ameren Companies' motion to consolidate the three dockets (05-0160/0161/0162 (Consol.)). The Commission entered an order to resuspend the tariffs on July 27, 2005. The Ameren Companies have filed the tariffs in anticipation of the end of the transition period provided for in the Electric Service Customer Choice and Rate Relief of 1997, 220 ILCS 5/16-101 et seq. (the "Restructuring Law") (see Section I.B for discussion of the Restructuring Law), which permitted each of the Ameren Companies to divest themselves of all or most of their generation assets during the transition period:

> AmerenCIPS and AmerenCILCO transferred their generation several years ago (except that AmerenCILCO retained ownership of several small (1 MW) power module units that are expected to be transferred out of AmerenCILCO before January 1, 2007.) AmerenIP transferred all of its generation before it was acquired by Ameren Corporation. Presently, each Ameren Company is served under a full requirements contract that expires at the end of 2006. Accordingly, each of the Ameren Companies must purchase its supply into order to provide any generation service.

(Resp. Ex. 1.0, pp. 4-5, lines 66-73)

To procure the power and energy necessary to serve their customers beginning January 1, 2007, the Companies' proposal relies as much as possible on a competitive bidding process — an auction — to secure commitments from suppliers to deliver "vertical tranches" of the Companies' load over the course of annual and multi-year contract terms. In particular, the Companies have proposed a competitive procurement process that uses a Simultaneous Descending Clock Auction ("SDCA"). (Resp. Ex. 6.0, pp. 14-15; ICC Staff Exhibit 1.0, pp. 6-11) Further, the Ameren Companies' proposal is designed to recover "the actual cost of power and energy procured." (Resp. Ex. 1.0, p. 3, lines 39-40)

The product that will be acquired in the SDCA is a full requirements product (i.e., an electricity product that provides the service components necessary to meet customer's instantaneous demand at any given time.) In the initial deployment of the Ameren Companies' proposed auction, the Auction Manager would be able to consider bids for various quantities of tranches (which constitute a fixed percentage of the Companies' load) in 1-year, 2-year, and 3-year supply contracts with the Ameren Companies.[1] The details of the proposed auction are contained in an Illinois Auction Rules manual (Resp. Ex. 19.3)

To comply with their obligations to continue to provide bundled service (i.e., including both electric supply and delivery) after January 1, 2007, the Companies have set forth Rider BGS ("Basic Generation Service") that will procure full requirements products via an auction based on three customer groups. Specifically, the Companies propose to use the filed auction process set forth in Rider MV to procure capacity, energy and other services from wholesale suppliers for three categories of full requirements products: (1) fixed-priced BGS for residential and small business customers ("BGS-FP") ; (2) fixed-priced BGS for large business customers ("BGS-LFP"); and (3) a fixed-price capacity product that, combined with spot purchases of energy from MISO, provides real-time pricing of energy for large business customers ("BGS-Large Service Real-Time Pricing" or "BGS -LRTP"). (Resp. Ex. 2.0 Corrected, p.

[1] Actually, the initial auction would be for 17-month, 29-month, and 41-month contacts so as to align the contract termination dates with the Midwest Independent Transmission System Operator, Inc . ("MISO") planning year which runs from June 1 to May 31. (Resp. Ex. 3.0, pp. 6-7, lines) Thereafter, an annual auction would replace expiring contracts with new 3-year contracts. The 1-year and 2-year contracts in the initial auction implement the 3-year auction cycle (i.e., with one-third of the Companies' loads being up for auction each year) so that contracts representing one-third of the Companies' load will expire each year.

18, lines 389-396) Rider BGS provides that the charges the various BGS customers shall pay for power and energy will be the prices defined in Rider MV. (See e.g., AmerenCIPS, Ill. C. C. No. 16, Original Sheet No. 22.001). Rider MV sets forth the methodology by which there is a translation of the procurement costs resulting from a competitive procurement process into seasonal and peak and off-peak values for use in calculating individual supply related charges in the Ameren Companies' retail tariffs, and describes the competitive procurement process for obtaining electric power and energy supply. (Resp. Ex. 4.0, pp. 5-6) In addition, Rider MV "provides for appropriate determination, on a periodic basis and in a transparent manner, of the market value of electric power and energy supply as a function of contracts applicable to the market in which the Company sells, and retail customers in its service area buy, electric power and energy." (AmerenCILCO, Ill. C. C. No. 18, Original Sheet No. 27.007; AmerenCIPS, Ill. C. C. No. 16, Original Sheet No. 27.007; AmerenIP, Ill. C. C. No. 35, Original Sheet No. 27.007).

With regard to the auction, the Ameren Companies have agreed to a joint auction to be held in the first 10 days of September with Commonwealth Edison Company ("ComEd") which has proposed a very similar procurement process in Docket 05-0159. (Resp. Exhibit 10.0 Corrected, pp. 14-15, lines 326-332) Further, the Ameren Companies and ComEd have agreed to allow bidders at the auction to switch between Comed's and the Ameren Companies' fixed price products (for the Ameren Companies, BGS-FP and BGS-LFP) and to switch between ComEd's and the Ameren Companies' hourly products (for the Ameren Companies, BGS-LRTP). However, there would be no switching between fixed price products and hourly products. (Resp. Ex. 12.0, p. 81, lines 1927-1929)

Also, with respect to the auction, the Ameren Companies have retained an Auction Manager (Dr. Chantale LaCasse, Resp. Ex. 6.0, 12.0 and 19.0) and have provided, in addition to testimony, the following: the Auction Manual (Rep Ex. 3.4), the Auction Rules (Resp. Ex. 19.3), Auction Timeline (Resp. Ex. 19.4), Part 1 and Part 2 Application Forms (Resp. Ex. 19.1 and 19.2) and Supplier Forward Contracts ("SFCs") (Resp. Ex. 12.4 and 19.2).

In response to the Company's filing, the following parties filed Petitions to Intervene, which were granted: Constellation NewEnergy, Inc.; Dynegy, Inc.; BlueStar Energy Services, Inc.; Citizens Utility Board ("CUB"); Illinois Industrial Energy Consumers; Commonwealth Edison Company; People of the State of Illinois ("AG"); People Energy Services Corporation; Environmental Law and Policy Center; Midwest Generation EME, LLC; Constellation Energy Commodities Group, Inc.; Morgan Stanley Capital Group, Inc.; J. Aron & Company; Direct Energy Services, LLC; MidAmerican Energy Company; United States Department of Energy; Midwest Independent Power Suppliers; Local Unions 15, 51 and 702, International Brotherhood of Electrical Workers, AFL-CIO; U.S. Energy Savings Corporation; Electric Power Supply Association; Illinois Energy Association; and Ameren Energy Marketing.

On behalf of Staff, the following witnesses submitted testimony: David J. Salant (ICC Staff Exhibit 1.0; ICC Staff Exhibit 11.0 Corrected), David S. Sibley (ICC Staff Exhibit 2.0-Revised), Richard J. Zuraski (ICC Staff Exhibit 3.0; ICC Staff Exhibit 12.0), Serhan Ogur (ICC Staff Exhibit 4.0, ICC Staff Exhibit 19.0), Eric P. Schlaf (ICC Staff

Exhibit 5.0; ICC Staff Exhibit 13.0), Peter Lazare (ICC Staff Exhibit 6.0; ICC Staff Exhibit 14.0), Cheri L. Harden (ICC Staff Exhibit 7.0), Rochelle Phipps (ICC Staff Exhibit 15.0), Mary E. Selvaggio (ICC Staff Exhibit 8.0; ICC Staff Exhibit 16.0), Scott A. Struck (ICC Staff Exhibit 9.0; ICC Staff Exhibit 17.0); and Steven R. Knepler (ICC Staff Exhibit 10.0; ICC Staff Exhibit 18.0).

In general, it is Staff's view that the Ameren Companies' Riders BGS and MV should be approved. However, Staff's recommendation for approval, as discussed below, has conditions and includes various changes and modifications to the Ameren Companies' proposal. Staff recommends that the Commission deny various Intervenor calls to reject the Companies' proposal as the Intervenors have failed to provide a sound or reasonable basis for such a rejection. (ICC Staff Exhibit 12.0, p. 3, lines 47-50) Further, as stated in "The Post-2006 Initiative: Final Staff Report to the Commission" released in November 2004, Staff believes that a vertical tranche auction provides a viable means of reaching the five policy goals of (1)"Mitigation of market structure problems"; (2) "Provision of regulatory certainty"; (3) "Provision of market based process and rate stability"; (4) "Provision of a straightforward mechanism to convert a wide variety of supply acquisition costs into retail rates using traditional rate design"; and (5) "Provision of a working option by January 2007." (ICC Staff Exhibit 12.0, pp. 4-5, lines 87-93)

B. Background

The Electric Service Customer Choice and Rate Relief Law of 1997 (the "Restructuring Law") implemented an unprecedented restructuring of the State's electric utility industry. Among other things, the Restructuring Law "initiated: (1) the opportunity for customers to purchase power from the supplier of their choice; (2) a restructuring of the State's electric power industry; and (3) a transition toward delivery service unbundling and greater reliance on market forces to determine how electric power and energy would be provided to retail customers who remain with the utility." (Resp. Ex. 2.0 Corrected, p. 5, lines 96-100) According to Ameren witness Nelson, this transition, brought on by the Restructuring Law, has had the following results so far:

- Residential customers have benefited from one of the largest and longest rate reductions, and today are paying 20% less than they paid for electricity in 1994. The total savings statewide are estimated to be 3.5 billion dollars.

- Many new entities have entered Illinois to compete for electric supply. Customers have been given the power of choice, and have selected these alternative retail electric suppliers ('ARES').

- Many industrial and commercial customers have realized significant savings from selecting the Power Purchase Option ('PPO') or an ARES; some indicate that these savings have helped them to keep their business in Illinois rather than move to a lower cost state.

- Statewide service reliability has improved dramatically.

- Over 9000 MWs of new generation has been built in Illinois by private investors. These investors, and not customers, have mustered the capital to build these plants and have borne the risk of cost overruns as well as the potential of uneconomic results in stranded costs.

- Illinois utilities have restructured operations by divesting generation, and have become more productive and efficient in order to face the emerging competitive marketplace.

(Resp. Ex. 2.0 Corrected, pp. 5-6, lines 104-124)

However, the transition period, during which retail rates have been frozen, is scheduled to end December 31, 2006. (Resp. Ex. 2.0 Corrected, p. 6, lines; see also 220 ILCS 106 5/16-111[2]) December 31, 2006 also marks “the end of the long-term supply contracts that most Illinois utilities entered into when, consistent with the Customer Choice Law's requirements and/or Illinois Commerce Commission ("Commission") rules, they sold or spun off their generating assets as part of the restructuring process.” (*Id.*, lines 129-132) Like other utilities, the Ameren Companies divested themselves of most of their generating assets:

> AmerenCIPS and AmerenCILCO transferred their generation several years ago (except that AmerenCILCO retained ownership of several small (1 MW) power module units that are expected to be transferred out of AmerenCILCO before January 1, 2007.) AmerenIP transferred all of its generation before it was acquired by Ameren Corporation. Presently, each Ameren Company is served under a full requirements contract that expires at the end of 2006. Accordingly, each of the Ameren Companies must purchase its supply into order to provide any generation service.

(Resp. Ex. 1.0, pp. 4-5, lines 66-73)

Thus, according to Mr. Nelson,

> [T]he Ameren Companies' current filing specifically addresses: (1) how they will procure power for their regulated service offerings to achieve the lowest possible, most competitive price; (2) how their bundled retail rates will be structured to result in stable but market-based prices; and (3) how they will recover their prudently-incurred, market-based procurement costs fairly from each customer class.

(Resp. Ex. 2.0 Corrected, p. 6, lines 137-142)

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[2] Although Section 16-111 includes provisions for such bundled rates to increase during the transition period, under certain circumstances, those circumstances have not materialized, to date, so rates have remain frozen.

II. NEED FOR COMMISSION ACTION

Staff believes it is appropriate for the Commission to act in this proceeding. Staff reserves the right to respond in its reply brief to parties that address this matter in their initial briefs.

III. LEGAL ISSUES

A. Background: the Illinois Electric Service Customer Choice and Rate Relief Law of 1997

See Section I.A, above.

B. ICC authority under Article IX and Article XVI to approve the filed tariffs

Section 9-201(c) of the Act provides in part that

> If the Commission enters upon a hearing concerning the propriety of any proposed rate or other charge, classification, contract, practice rule or regulation, the Commission shall establish the rates or other charges, classifications, contracts practices, rules or regulations proposed, in whole and in part, or others in lieu thereof, which it shall find to be just and reasonable. … (220 ILCS 5/9-201(c))

Thus, the Legislature has granted the Commission the authority to enter into hearings with respect to tariffs that a utility has filed pursuant to Section 9-201 of the Act and to establish rates that it finds to be just and reasonable. Prior to 1997, electric utilities, such as the Ameren Companies, generally owned their own generating assets that produced the power and energy needed to serve their customers. As a result, the tariffs typically filed by electric utilities in that time period pursuant to Section 9-201 of the Act would seek to recover the costs related to the generating assets that were used to provide service to customers.

However, starting in 1997, the manner which electric utilities would obtain power and energy to meet their customers' needs changed. The Electric Service Customer Choice and Rate Relief Law of 1997 (the "Restructuring Law") was a massive overhaul of the State of Illinois' policy toward electric utility service. It began a transition toward delivery service unbundling and greater reliance on market forces to determine how electric power and energy would be provided to retail customers. (The Post 2006 Initiative: Final Staff Report to the Commission, December 2, 2004, p. 1) The Restructuring Law was codified in Article XVI of the Act. (220 ILCS 5/16-101 et seq.)

Section 16-111(i) of the Act provides in part:

> Subsequent to the mandatory transition period, the Commission, in any proceeding to establish rates and charges for tariffed services offered by an electric utility, shall consider only (1) the then current or projected revenues, costs investments and cost of capital directly or indirectly associated with the provision of such tariffed services; … In determining the just and reasonableness of the electric power and energy component of an electric utility's rates for tariffed services subsequent to the mandatory transition period and prior to the time that the provision of such electric power and energy is declared competitive, the Commission shall consider the extent to which the electric utility's tariffed rates for such component for each customer class exceed the market value determined pursuant to Section 16-112, …

220 ILCS 5/16-111(i).

Section 16-112(a) of the Act in turn states:

> The market value to be used in the calculation of transition charges as defined in Section 16-102 shall be determined in accordance with either (i) a tariff that has been filed by the electric utility with the Commission pursuant to Article IX of this Act and that provides for a determination of the market value for electric power and energy as a function of an exchange traded or other market traded index, options or futures contract or contracts applicable to the market in which the utility sells, and the customers in its service area buy, electric power and energy, or (ii) in the event no such tariff has been placed into effect for the electric utility, or in the event such tariff does not establish market values for each of the years specified in the neutral fact-finder process described in subsections (b) through (h) of this Section, a tariff incorporating the market values

> resulting from the neutral fact-finder process set forth in subsections (b) through (h) of this Section.

220 ILCS 5/16-112(a) (footnote omitted).

Thus, pursuant to Section 16-111(i), it is within the Commission's authority to review a competitive procurement process-driven tariff such as the Ameren Companies' filed tariffs. (Memorandum to the Commission from Philip A. Casey, November 23, 2004, Subject: OGC Comment and Analysis on Working Group Implementation Reports). Such tariffs must clear at least two hurdles: (1) FERC regulation, including strictures governing wholesale electric transactions between sellers of electricity and affiliated wholesale purchasers, and (2) the provisions of the Public Utilities Act relevant to the setting of rates after 2006 including Article IX, and Section 16-111(i) of the Act, with its directive that the Commission consider the extent to which the power and energy component of rates exceeds the market value determined pursuant to Section 16-112 of the Act. (OGC Comments on Procurement Working Group Implementation Report ("PWGIR"), p. 1)

With respect to the first hurdle, the Commission "may retain jurisdiction to review rates including FERC-jurisdictional prices, as permitted by federal law, e.g. under the 'Pike County' doctrine'. (RWG Final Report, pp. 16-17 (in discussion of Scenario 4) quoting *Pike County Light & Power Co. v. Pennsylvania Public Utility Comm'n*, 465 A.2d 735 (Comm. Ct. of Pa. 1983))

With respect to the second hurdle which relates to the establishment of rates subsequent to the mandatory transition period for the electric power and energy component of non-competitive services, Section 16-111(i) of the Act requires the Commission to "consider the extent to which the electric utility's tariffed rates for such component for each customer class exceed the market value determined pursuant to Section 16-112". (220 ILCS 5/16-111(i)) The Commission is also authorized to impose a rate ceiling in the event the rates[3] for that electric power and energy component exceed the market value by more than 10%. *Id*. Thus, in order for post-transition period rates to comply with Section 16-111(i) of the Act, the utility must provide or propose some method to compare its proposed rates to the market value determined pursuant to Section 16-112 of the Act. The Ameren Companies' proposal was clearly intended to provide such a method.

The Ameren Companies have filed their proposed tariffs pursuant to 16-112(a). (Ameren Companies Supplemental Information, pp. 4-6; see e.g., AmerenCIPS, Ill. C.C. No. 16, Original Sheet No. 27.005) Whether those tariffs meet the requirements of 16-112(a), i.e. the tariff "provides for a determination of the market value for electric power and energy as a function of an exchange traded or other market traded index, options or futures contract or contracts applicable to the market in which the utility sells, and the customers in its service area buy, electric power and energy", is a question of fact. As explained in this brief, the Commission should find that the Companies meet this requirement based on the evidence and arguments submitted in this matter.

Further, the fact that the Ameren Companies' Rider MV establishes formula based rates does not diminish Commission authority. Formula based rates have been used on prior occasion by utilities in Illinois and approved by Illinois courts. (See *City of Chicago v. Illinois Commerce Comm'n*, 13 Ill.2d 607, 150 NE.2d 776 (1958)) "Certainly

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[3] The rates for electric power and energy must be just and reasonable, as required by Sections 9-101 and 9-201 of the Act. 220 ILCS 5/9-101, 9-201.

there are provisions in Articles IX and XVI that can be interpreted as permitting the adoption of tariffs that stop short of expressing charges on the basis of cents or dollars per unit of commodity or service. Also, any tariff that would express electricity charges in terms of the unknown outcome of a competitive procurement process would, as a prerequisite to enforceability, have to have been determined by the Commission to be consistent with the provisions of Article XVI." (OGC Comments on PWGIR, p. 4) Thus, the Commission has the authority to approve formula-based rates.

Additionally, despite the fact that residential and small business services have not been ruled competitive, the Commission has authority to rule on the Ameren Companies' tariffs. Section 16-103(c), which addresses residential and small business services, provides as follows:

> (c) Notwithstanding any other provision of this Article, each electric utility shall continue offering to all **residential customers** and to all **small commercial retail customers** in its service area, as a tariffed service, bundled electric power and energy delivered to the customer's premises consistent with the bundled utility service provided by the electric utility on the effective date of this amendatory Act of 1997. Upon declaration of the provision of electric power and energy as competitive, the electric utility shall continue to offer to **such customers**, as a tariffed service, bundled service options at rates which reflect recovery of all cost components for providing the service. For those components of the service which have been declared competitive, cost shall be the market based prices. Market based prices as referred to herein shall mean, for electric power and energy, either (i) those prices for electric power and energy determined as provided in Section 16-112, or (ii) the electric utility's cost of obtaining the electric power and energy at wholesale through a competitive bidding or other arms-length acquisition process.

220 ILCS 5/16-103(c) (emphasis added). Although Section 16-103(c) allows and addresses market-based rates for competitive services, Section 16-103(c) is a limitation on the ability of electric utilities to set market-based rates. The grant of authority to set

market-based rates for all retail competitive services is found in Section 16-103(a) of the Act, which provides, in its entirety, as follows:

> (a) An electric utility shall continue offering to retail customers each tariffed service that it offered as a distinct and identifiable service on the effective date of this amendatory Act of 1997 until the service is (i) declared competitive pursuant to Section 16-113, or (ii) abandoned pursuant to Section 8-508. Nothing in this subsection shall be construed as limiting an electric utility's right to propose, or the Commission's power to approve, allow or order modifications in the rates, terms and conditions for such services pursuant to Article IX or Section 16-111 of this Act.

220 ILCS 5/16-103(a). Thus, subject to limitations stated elsewhere in the Restructuring Law, an electric utility is relieved of its obligation to provide retail services offered at the time of enactment of the Restructuring Law when "the service is . . . declared competitive pursuant to Section 16-113 . . . ." (Id.) Once so relieved of its provider of last resort obligations, an electric utility is free to charge market rates subject to any limitations stated elsewhere in the Act.

As stated above, one such limitation is set forth in Section 16-103(c) of the Act, which places limits on the rates that a utility may charge competitive residential and small business services by requiring the continued offering of tariffed services for such customers "at rates which reflect recovery of all cost components for providing the service . . . ." While Section 16-103(c) of the Act refers to "market-based prices", this phrase is used in defining "costs" and it is clear from the statutory language of Section 16-103(c) that the Legislature did not consider "market-based prices" and "cost-based rates" to be mutually exclusive concepts. Rather, Section 16-103(c) indicates that the rates for certain competitive services must "reflect recovery of all **costs components** for providing the service" and that "**costs** shall be the market based prices . . . " which are specifically defined as "either (i) those prices for electric power and energy determined as provided in Section 16-112, or (ii) the **electric utility's cost** of obtaining the electric power and energy at wholesale through a competitive bidding or other arms-length acquisition process.". (220 ILCS 5/16-103(c) (emphasis added)) Thus, it is clear from the language of Section 16-103(c) that "market-based prices" as used in Section 16-103(c) may be determined based on the utilities' actual cost of obtaining such power and energy through any arms-length acquisition process – including a competitive bidding process.

Thus, Section 16-103(c) of the Act imposes a limitation on market rates that allows either a market-value rate under Section 16-112 of the Act or a cost-based rate. Since the Ameren Companies no longer possess their own generation assets (Resp. Ex. 1.0, p. 3), the only means for the Ameren Companies to acquire the electric supply they need to serve their customers is through third party suppliers. Based on Section 16-103(c), the Commission may set rates based on the costs incurred through the only means available to the Ameren Companies to obtain such supply.

Furthermore, the explicit language contained in Section 16-103(a) provides that "[n]othing in this subsection shall be construed as limiting an electric utility's right to propose, or the Commission's power to approve, allow or order modifications in the rates, terms and conditions for such services pursuant to Article IX or Section 16-111 of this Act.". (220 ILCS 5/16-103(a)) Section 16-103(c) is a limitation on the Legislature's decision to generally relieve electric utilities of their obligation to provide services that are declared competitive. The Legislature has specifically directed that nothing with respect to its decision to remove competitive services from traditional regulatory oversight shall be interpreted or construed to limit the Commission's authority or power pursuant to Article IX or Section 16-111.

Finally, the declaration of findings contained in the Restructuring Law makes clear that the Legislature acknowledged that "[c]ompetitive forces are affecting the market for electricity" and that it intended for the Commission to "promote the development of an effectively competitive electricity market that operates efficiently and is equitable to all consumers." (220 ILCS 5/16-101A(b)) Although such provisions do not constitute substantive provisions of the Act (*See Governor's Office of Consumer Services v. Illinois Commerce Commission*, 220 Ill. App. 3d 68, 74 (3rd Dist. 1991); *Monarch Gas Co. v. Illinois Commerce Commission*, 261 Ill. App. 3d 94, 99 (5th Dist. 1994)), the language supports the Ameren Companies' proposal under investigation in this docket. The proposed Rider MV clearly acknowledges competitive developments and is consistent with the development of competitive markets and proposes protections for consumers and others.

C. Relationship of Illinois and federal law and jurisdiction

Staff believes that the Companies' proposal is consistent with applicable Illinois and federal jurisdictional limits. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

D. References to Post 2006 Initiative reports and results

Staff addressed this issue in Response Of The Staff Of The Illinois Commerce Commission To Motion In Limine To Exclude Testimony Regarding The Post 2006

Workshops By The People Of The State Of Illinois, The Citizens Utility Board, And Environmental Law And Policy Center Of The Midwest ("Staff Response to Motion to Strike") filed September 12, 2005. References to the Post-2006 Initiative reports and results contained in Staff's testimony are appropriate, and the Administrative Law Judge ("ALJ") appropriately denied the motion. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

E. Evidentiary issues

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

F. Other legal issues

Staff reserves the right to respond in its reply brief to parties who raise other legal issues in their initial briefs.

IV. SUFFICIENCY OF THE COMPETITIVE MARKET

A. Markets' relationship to auction process

Witnesses for the AG and CUB testified that the underlying wholesale market was not sufficiently competitive for the Ameren Companies to rely upon it for acquiring power and energy at reasonable prices. For example, AG witness Rose stated,

> If there were an insufficient number of suppliers or there is inadequate transmission access to import electricity into the Ameren service territory, it is possible that one supplier or a small group of suppliers would be able to have some degree of control over the wholesale market price. That is, these suppliers would be able to exercise market power. If this were to occur, auction prices would be higher than what would occur in a more

> competitive market – with more suppliers and better access to transmission.

(AG Ex. 1, p. 5) Furthermore, among Dr. Rose's conclusions were:

> 1) The wholesale electricity market in and around Illinois is not sufficiently developed, at this time, to ensure a level of competition among suppliers that would yield competitive prices. Given the current state of the wholesale electricity market in the region and its stage of development, it is premature to use an auction process, like the one proposed by Ameren, to procure electricity for retail customers.
>
> 2) Implementing a market-based approach to procurement and ratemaking, before the wholesale market is sufficiently developed, will be harmful to retail customers – who will face higher rates than under alternative, cost-based approaches.

(AG Ex. 1, p. 30, lines 2-13)

Inexplicably, Dr. Rose also addressed the "Competitiveness of Retail Markets," stating, for example:

> Many retail markets have remained relatively inactive, particularly for smaller residential customers. In some states, market activity for larger customers has been somewhat more active.

(*Id.*, p. 19, lines 17-19) However, it is self-evident that any deficiencies in the competitiveness of the ***retail*** electricity markets merely add to the urgency and importance of approving viable and appropriate procurement methods for electric utilities to implement, since consumers who cannot rely on a competitive ***retail*** market should at least be able to rely upon their regulated public utilities to supply them with electric power. Deficiencies in the competitiveness of ***retail*** electricity markets, in and of themselves, say absolutely nothing about which procurement methods are appropriate for electric utilities to implement.

In addition to the AG witnesses, CUB witnesses Fagan and Steinhurst also expressed concerns about the wholesale market for electricity (CUB Exhibit 1.0; and CUB Exhibit 2.0, pp. 11-12).

Staff expects that Ameren will try to demonstrate in its own brief that many of the AG and CUB concerns were shown by Ameren witness Frame to be exaggerated or unfounded. Staff also expects that the Ameren Companies will try to demonstrate that, with RTO and FERC oversight, the electric wholesale market is competitive enough that it can be relied upon as the sole source for utilities to obtain least-cost electric supply for retail customers. But Staff is not convinced that such demonstrations are entirely warranted or useful to the Commission in the context of this docket. In Staff's view, assessing the competitiveness of electricity markets is pertinent to a broad debate about policies toward the electric industry; but it is not directly pertinent to a debate over how electric utilities in Illinois will acquire electric power to sell to their retail customers starting in 2007. As Staff witness Zuraski testified,

> I am not going to comment directly on the competitiveness of the wholesale market for electricity. However, even assuming, for the sake of argument, that the wholesale market is not competitive, that would not change the facts that (i) Ameren has an obligation to provide power and energy to most of its retail customers and (ii) the only conceivable place that Ameren will be able to acquire power and energy for delivery beginning in 2007 is the wholesale market. Furthermore, even if the wholesale market is not competitive, Mr. Fagan and Dr. Steinhurst have not explained why the NJ model should be rejected. That is, they have not explained how an alternative procurement process would somehow circumvent a less-than-competitive wholesale market and produce a more favorable result for ratepayers.

(ICC Staff Exhibit 12.0, p. 8, lines 163-173)

Ameren witness Frame seemed to have a similar opinion about the relevance of these AG and CUB topics. (see, for example, Resp. Ex. 13.0, p. 3 ,lines 62-66; p. 10, lines 229-234; p. 17 lines 378-385; and pp. 17-18, lines 386-394)

In Staff's view, what is more enlightening is the testimony that the AG and CUB witnesses did ***not*** provide. As noted in Mr. Nelson's rebuttal testimony:

> Q. Does CUB offer a meaningful alternative solution to the Ameren Companies' need to procure power?
>
> A. No, it does not.

(Resp. Ex. 10.0 Corrected, p. 32, lines 729-731)

Mr. Nelson offered the same assessment of AG witness Salgo's testimony (Resp. Ex. 10.0 Corrected, p. 29, lines 660-666), while Dr. Frame said as much about AG witness Rose's testimony. (Resp. Ex. 13.0, pp. 19-20, lines 423-430)

Thus, even if the AG and CUB witnesses' concerns with the competitiveness of the electricity market were fully justified, those concerns would not help the Commission choose a better method for procuring power and energy for retail customers. To be fair, the AG and CUB witnesses at least provided some rough sketches of alternative procurement proposals, which will be the subject of Section VI. "Procurement processes alternatives." For now, suffice it to say that those alternatives (i) still rely upon the same wholesale market, (ii) involve actions arguably outside the scope of the Commission's jurisdiction, (iii) involve actions arguably contrary to Illinois statutes, or (iv) are simply too vague and incomplete. Perhaps the least vague, incomplete alternative was Dr. Steinhurst's terse recommendation to

> … reject the competitive procurement and require Ameren to procure least cost power under traditional cost recovery standards. Such procurement would be subject to traditional ratemaking standards.

(CUB Exhibit 2.0, p. 18, lines 393-395)

However, as Staff witness Zuraski replied,

> I have to disagree with rejecting "competitive procurement" in favor of such a vague alternative…. Indeed, it is unclear if Dr. Steinhurst's proposed alternative is even different than "competitive procurement." First, "to procure least cost power" is a goal and not a procurement method or process. Second, that goal is not inconsistent with using a competitive procurement process. Third, Dr. Steinhurst not only fails to explain what he means by "traditional rate making standards", but he also fails to explain how using an auction or using a translation tariff is inconsistent with such traditional standards. In short, there is no basis for the Commission to accept Dr. Steinhurst's recommendations, because they lack substance.

(ICC Staff Exhibit 12.0, p. 6, lines 120-131)

In conclusion, Staff recognizes that parties have concerns about the competitiveness of wholesale electricity markets. However, Staff does not see how those concerns eliminate the need for utilities to acquire power and energy from those wholesale markets. Staff recognizes that parties have concerns about the competitiveness of retail electricity markets, but this increases rather than decreases the need to approve viable and appropriate procurement methods for electric utilities to implement. Finally, among the legislative findings of the Restructuring Law is that

> Competitive forces are affecting the market for electricity as a result of recent federal regulatory and statutory changes and the activities of other states. Competition in the electric services market may create opportunities for new products and services for customers and lower costs for users of electricity. Long-standing regulatory relationships need to be altered to accommodate the competition that could fundamentally alter the structure of the electric services market.

(220 ILCS 5/16-101A (b))

Manifestly in pursuit of this policy goal, the Restructuring Law permitted and facilitated the divestiture of utility generation assets, and defined a "mandatory transition period" that runs through January 1, 2007. (220 ILCS 5/16-111(g); 220 ILCS 5/16-102)

It is no surprise, and has been no secret, that Ameren's existing supply contracts expire December 31, 2006, and "the clock has been and continues to be ticking, bringing us closer to the post 2006 era." (ICC Staff Exhibit 12.0, p. 4, lines 56-57) The Commission does not have the luxury of reassessing, let alone unraveling, the General Assembly's decision to enact the Restructuring Law. That is a legislative matter and not a matter for this administrative agency to ponder. The Commission should seek to ensure a viable procurement approach, and in Staff's view, the only viable approaches, at least in the near term, will rely on the wholesale market.

B. Other jurisdictions' experiences with competitive electricity procurement

With respect to other jurisdictions' experiences with competitive electricity procurement, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties that address this matter in their initial briefs.

C. Retail market conditions

With respect to retail market conditions, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

D. Relevant product market

1. Required products

With respect to required products, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

2. Physical vs. financial markets

With respect to physical vs. financial markets, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

3. MISO capacity market

With respect to the MISO capacity market, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

E. Relevant geographic market

1. Significance of political boundaries

With respect to the significance of political boundaries, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

2. MISO/PJM seam & Joint Operating Agreement

With respect to MISO/PJM seam & Joint Operating Agreement, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

F. Market characteristics, including supplier concentration

With respect to market characteristics, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

G. Transmission constraints

With respect to transmission constraints, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

H. Limitations on generator entry

With respect to limitations on generator entry, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

I. Relationship to service to small commercial and residential customers

With respect to relationship to service to small commercial and residential customers, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

J. Market rules and monitoring

1. MISO market rules

With respect to MISO market rules, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

2. MISO Market Monitoring Unit ("MMU")

With respect to MISO MMU, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

3. Proposed Illinois Market Monitor

With respect to the proposed Illinois Market Monitor, see Staff discussion in sub-section A above. Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

K. Other competitive market issues

Staff has nothing to add at this time, but reserves the right to respond in its reply brief to parties who introduce other competitive market issues in their initial briefs.

V. AUCTION DESIGN ISSUES

As noted in Section I, above, the Ameren Companies propose to meet their obligation to provide power and energy to most of their retail customers after the Transition Period by relying as much as possible on commitments from wholesale suppliers to deliver "vertical tranches" of the utilities' full requirements load, secured through a particular type of competitive bidding process, which Staff refers to as a simultaneous descending clock auction ("SDCA"). These commitments would be for periods as short as one year and as long as three years.[4] This section of Staff's brief discusses the mechanics of the auction, the products up for auction, the contracts that the Ameren Companies propose to enter into with suppliers of the auction products, and the contingency plans that the Ameren Companies would implement if such contracts turn out to be insufficient to satisfy the entire load.

A. General effectiveness and suitability

The Ameren Companies propose to utilize a variant of a "simultaneous multiple round auction," using a "descending clock" format (Resp. Exhibit 6.0, pp. 14-15), which

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[4] In the initial deployment of the auction, five months are added on to the start of the contracts to cover the period from January through May 2007.

has also been called a "simultaneous descending clock auction" (ICC Staff Exhibit 1.0, pp. 6-11). The primary features of the SDCA are as follows:

- It is a simultaneous auction in that multiple products are auctioned at once. For example, in the utilities' proposal, as modified in their rebuttal testimony, fixed-price (dollars per KWH) contracts to serve ComEd load and Ameren load, to serve such load through different durations, and to serve different customer load groups are all auctioned simultaneously, allowing bidders to switch between products during the auction.

- It is a descending clock auction in that prices start high and tick down over time during the course of the auction. In this type of auction, at each point on the price clock (in each round of bidding), suppliers bid the quantity of tranches that they are willing to serve at the announced prices. Bidding continues until supply for each product equals demand.

- The winning bidders for the various products pay the auction-clearing prices for those prices.

Ameren witness LaCasse discussed several advantages to using this type of auction over requests for proposals ("RFPs") and other auction formats.

She noted that the SDCA is an example of an "open auction," which features multiple rounds "so that bidders learn and can re-adjust their bids as the auction proceeds." (Resp. Ex. 6.0, p. 15, lines 338-340) She explained further:

> [O]pen auctions are likely to provide important economic benefits in contexts such as BGS procurement for the Illinois utilities and open auctions are likely to have significant advantages over the use of a sealed bid ("RFP") process.

(*Id.*, p. 16, lines 364-367)

Such benefits of the open action include:

> [B]idders are provided with market information round by round. … [and have the flexibility] to re-adjust their bids in the light of new information. … Receiving market information round-by-round is valuable because all bidders are independently assessing similar market risks and opportunities. … The flexibility to re-adjust bids takes away some of the guess work in bidding that is present in an RFP. When bidders face less

uncertainty and guesswork, bidders have more confidence and tend to bid more aggressively. Bidders tend to be more willing to supply at lower prices. This aggressive bidding results in prices that are more competitive and better for consumers. This is an important economic benefit of open auctions in this context. …

Because the auction ends when bidders are no longer willing to better their offers, the bidders who do win at the end of the auction are those that are willing to serve the load at the lowest prices. …

When several related products are included in the same auction, one economic benefit of the use of open auctions is that the prices that are set will be reflective of the market. In an open auction, bidders see the prices as they tick down every round. Bidders can, in response to those prices, switch their bids from one product to another. The switching means that the auction sets price differentials that are rational and market-driven. …

A final economic benefit of the open auction when there are several related products is that the allocation of supply responsibility over the various products proposed by Ameren to serve the load of BGS customers is likely to be efficient.

(*Id.*, pp. 16-18, lines 368-396; p. 18, lines 398-400; pp. 19-20, lines 435-440; p. 20, lines 453-455)

In addition,

The clock auction format is transparent and maximizes participation. Bidders can clearly understand how the final auction price is determined and how winning bidders emerge. The fact that the format does not advantage established players can encourage smaller or newer bidders to participate. …

The clock auction is inherently a flexible auction format. It can accommodate, in one simultaneous auction, products of different terms, products for different EDCs, or products for different customers segments. The clock auction is an essential element of preserving the flexibility of the process and of accommodating future refinements. …

The clock auction also helps ensure that all products are subscribed, even if there are several small products that may not have attracted as much interest on their own. In the clock auction format, all products can be put at auction at once so that the broadest range of interest is attracted to the auction, and invited to bid even on smaller products. As the price tick down, if a smaller product's price remains high for a time, it will attract bids and its price too will tick down.…

> The rules are well specified and the bidders will be able to clearly understand how the final auction price is determined and how winning bidders emerge…
>
> (*Id.*, p. 35, lines 794-797; p. 36, lines 812-815; pp. 36-37, lines 816-821; p. 84, lines 1895-1896)

Dr. LaCasse also noted that, since 2000, over twenty open auctions have been conducted in the energy sector around the world. This includes the electric distribution companies in New Jersey, which have held simultaneous descending clock auctions to procure full-requirements supply for their basic generation customers in each of 2002, 2003, 2004, and 2005. (*Id.*, p. 15-16, lines 345-351) Other Ameren witnesses supporting this basic auction design were Mr. Pfeifenberger (Resp. Ex. 7.0) and Mr. Blessing (Resp. Ex. 3.0, p. 28).

Staff witness Salant agreed that the SDCA is an appropriate mechanism for an Illinois competitive power procurement process:

> [A] significant literature exists in the field of economics that analyzes the advantages and disadvantages of the SMR auction format and its variants (including the SDCA) under different circumstances. … In general, the economics literature and the global experience with the SMR auction format supports Ameren's proposal to use the SDCA for electricity procurement.

(ICC Staff Exhibit 1.0, pp. 12-13, lines 274-282)

However, other parties presented evidence questioning the use of the basic SDCA format. These criticisms of the SDCA format came in two basic forms. First, there was testimony either implying or contending that no competitive procurement process should be utilized. (CUB witnesses Fagan and Steinhurst; and AG witnesses Rose and Salgo) These critiques will be addressed in Section VI "Procurement Process Alternatives." Second, there was testimony that another auction format can perform better than the SDCA. (AG witness Reny) The Reny critique of the SDCA, as well as his alternative auction format, will be addressed under sub-section D. "Clearing Price: Uniform versus pay-as-bid." As will be argued in detail, the above-referenced critiques do not persuasively support a rejection of the basic SDCA design. Furthermore, the record in the case provides no better (or even barely adequate) alternatives to the SDCA proposal presented by Ameren.

In summary, Staff concludes that the basic SDCA auction concept, as proposed by the Ameren Companies and endorsed by Staff witness Salant, is an appropriate competitive procurement method for securing power supply commitments for serving Ameren's retail customers. Hence, Staff respectfully recommends that the Commission approve the basic SDCA approach. In making this recommendation with respect to the basic SDCA approach, Staff is not tacitly endorsing other aspects of the proposed auction process or other aspects of the Ameren Companies' proposal in this case.

B. Full requirements product

As noted above, the Ameren Companies propose to acquire commitments from suppliers to provide "vertical tranches" (or fixed percentages) of the Ameren Utilities' entire full requirements load, as that load varies over time. "Tranche" is a French word meaning slice. Defining the basic product as a slice of full requirements essentially removes the burden of generation portfolio decision making from the shoulders of the utilities (and to some extent, the Commission) and places it on the shoulders of suppliers, instead. This is an obvious change from the traditional role of the typical utility company, which acquired its own fleet of generators to meet the needs of its customers. However, it is very similar to the type of full-requirement product that each of the Ameren Companies currently purchases from wholesale suppliers.

Alternatives to procuring vertical tranches of the full requirements load would entail procuring an appropriate array of specific types of supply contracts and/or generating assets (e.g., an appropriate assortment of contracts or assets designed to serve base-load, intermediate-load, and peaking-load). Although some intervenors in this docket proposed considering such “active portfolio management” alternatives, Staff opposes them for reasons that will be discussed more fully below, in section VI. In contrast, Staff supports the vertical tranche concept since, as articulated by Ameren witness LaCasse (Resp. Ex. 6.0, pp. 30-31, lines 678-700):

> - The full-requirements product directly contributes to fulfilling the goal of having competitive entities take, manage and price BGS risks. The full-requirements product places price-risk management responsibility in the hands of competitive entities that were best suited to take, manage, and price these risks. This would ensure that customers receive for these services a price that was disciplined by competitive forces. This would also help assure that these services can be provided as efficiently as possible, with each supplier free to hedge or meet requirements in any way that it chose, rather than being limited by regulatory review.
>
> - The full-requirements product contributes to the goal of maximizing participation. It expands the base of potential competitors, including financial players and marketers and traders without an asset base in PJM. Those entities are able to use specialized skills in price-risk management to assemble wholesale portfolios and compete in the auction. Resp. Exs. 6.3 and 6.4 to this testimony summarize the participation in the auction and document the fact that participation has not been limited to portfolio owners in the regions, but has instead included a broad base of suppliers, including marketers and traders, and financial players.
>
> - A full-requirements product also avoids customer confusion by obtaining a market-priced fixed price service for customers so that customers can reasonably budget for energy usage.

- The full-requirements product also contributes to the goal of encouraging efficient retail markets. The price against which customers will evaluate competitive offers, the BGS price, is established and known in advance. Furthermore, it is set at a market level that includes all wholesale supply costs and risks.

Thus, Staff respectfully recommends that the Commission approve the basic full-requirements product concept in this docket. In making this recommendation with respect to the basic full-requirements product concept, Staff is not tacitly endorsing other aspects of the proposed auction process or other aspects of Ameren's proposal in this case.

C. Multiple round descending clock format

1. Load caps

Ameren witness LaCasse indicated that Ameren's auction proposal contains four "competitive safeguards." (Resp. Ex. 6.0, pp. 42-47) One of these purported safeguards is a "load cap." The Ameren Companies' original proposal included a recommendation for a load cap of 50%. That is, the Companies proposed that no single bidding supplier would be permitted to win more than 50% of the tranches sought by each utility company per auction.

The rationale for a load cap was articulated by Dr. LaCasse as follows:

> The load cap both limits the influence that any one bidder can have on the results of the auction and acts as a complement to the provisions for volume reduction (the first competitive safeguard).

(Resp. Ex. 6.0, p. 45, lines 1013-1015)

Ameren witness Nelson added that load caps "diversify the exposure of the Ameren Companies to any one particular supplier's contract and credit risks, by preventing the supply agreements from being concentrated in a few large suppliers." (Resp. Ex. 10.0 Corrected, p. 9, lines 207-209)

As for the specific load cap of 50%, Dr. LaCasse explained:

> In my opinion, the combination proposed by Ameren of a 50% load cap together with limiting information regarding the remaining excess supply in each segment but only when bidding nears its conclusion strikes the right balance. This combination should be effective in limiting the influence of a bidder or a small group of bidders on the auction results while providing information to bidders on a round-to-round basis to enable bidders to revise their bids and learn on the basis of the information available to them.

(Resp. Ex. 6.0, p. 51, lines 1156-1162)

While the rationale for load caps was echoed by Staff witnesses Salant and Sibley (ICC Staff Exhibit 1.0, pp. 57-60; ICC Staff Ex. 2.0 Revised, pp. 20-21), these and other witnesses questioned the Ameren Companies' specific proposal to set the load cap at 50% of the tranches sought by each utility company per auction. (ICC Staff Exhibit 1.0, pp. 65-69; ICC Staff Exhibit 2.0 Revised, pp. 25-27; IIEC Exhibit 3, pp. 6-14). For example, Professor Sibley observed that Ameren did not address several important questions regarding load caps:

- Why should the level of the load caps in Illinois be 50 percent? In her testimony, Dr. LaCasse argues that a load cap "limits the scope of anti-competitive behavior in the auction." (Docket Nos. 05-0160, 05-0161 and 05-0162 Consolidated, Exhibits 6.0, p. 45.) However, Dr. LaCasse fails to demonstrate how Ameren's proposed 50 percent load cap limits the scope of anticompetitive behavior in its auction. Ultimately, Ameren's proposal provides no justification for a 50 percent load cap.

- The load caps in New Jersey are 30 to 35 percent. In light of the weight given by Dr. LaCasse to the New Jersey BGS experience, why are the load caps in Illinois different than those in New Jersey? In particular, what are the differences between Illinois and New Jersey that justify a higher load cap in Illinois?

- Does it matter what a large supplier does with supply that it wants to sell in the auction, but which exceeds the load cap? What if a large supplier is also a low-cost supplier (as is likely the case in Illinois)? Under what terms, if any, should such a supplier be allowed to sell its extra capacity in the auction?

(ICC Staff Exhibit 2.0 Revised, pp. 23-24, lines 392-408)

Staff witness Salant proposed to set the cap within the range of 25-35 percent. (ICC Staff Exhibit 1.0, pp. 69-70) IIEC witness Collins recommended eliminating the cap altogether, which amounts to setting it at 100%. (IIEC Exhibit 3, p. 14)

In support of Staff's proposal, Dr. Salant argued, "Absent a detailed analysis of the optimal load cap for the Illinois CPP, I recommend setting the load cap at a level consistent with the levels used in previous SMR format auctions, i.e., in the range of 25 to 35 percent." (ICC Staff Exhibit 1.0, p. 70, lines 1574-1577) Professor Sibley supported this recommendation, testifying as follows:

> I note that Dr. Salant's alternative proposal (see ICC Staff Exhibit 1.0) regarding load caps is likely to result in a more competitive auction, and hence in lower prices for Illinois ratepayers as compared to Ameren's proposed 50 percent load caps.

(ICC Staff Exhibit 2.0 Revised, p. 28, lines 499-502)

In rebuttal testimony, the Ameren Companies agreed to a load cap of 35% (which is at the upper end of Dr. Salant's proposed range). Ameren witness Nelson summarized the revised load cap proposal as follows:

> [T]he Ameren Companies have modified the proposed load cap level in response to the concerns raised by the parties. The Ameren Companies now propose a 35 % load cap by auction section (instead of the 50 % load cap by segment as initially proposed).

(Resp. Ex. 10.0 Corrected, p. 11, lines 251-254)

The Ameren Companies' revised load cap was supported by Staff witness Salant in rebuttal testimony. (ICC Staff Exhibit 11.0 Corrected, p. 7, lines 151-154)

Ameren witness LaCasse sanctioned the change, as well, concluding,

> I believe that a load cap set in the 33% to 50% range will be effective in providing a degree of supplier diversification, in reducing incentives to withdraw strategically, in reducing incentives to overstate interest, while not overly constraining the participation of the bulk of the anticipated pool of bidders.

(Resp. Ex. 12.0, p. 63, lines 1489-1492)

In contrast, Dr. LaCasse rejected IIEC witness Collins' recommended elimination of the load cap, testifying as follows:

> Mr. Collins considers only one of the four factors that are relevant to evaluating the level of the load cap. He rightly points out that a higher load cap – and 100% is as high as a load cap gets – has the potential benefit of providing additional opportunities for some entities to bid in a greater amount of supply. However, this is only one side of the equation. Mr. Collins does not take into account that a 100% load cap has real costs. A 100% load cap would remove the needed discipline on bidders' ability to over-represent their interest in the auction, remove the needed discipline on a single bidder's ability to influence the auction results, and provide no assurance whatsoever of diversification of the supplier base. A 100% load cap strips the auction of essential protections against bidder strategies that can lead to higher auction prices.

(Resp. Ex. 12.0, p. 30, lines 737-747) Staff concurs with Dr. LaCasse's arguments against elimination of the load cap.

In conclusion, Staff notes that the weight of the evidence supports the Ameren Companies' rebuttal-stage 35% load cap proposal. Further, it is within the range recommended by Staff witness Salant and by Ameren witness LaCasse. Thus, Staff respectfully recommends that the Commission reject the IIEC proposal for the elimination of the load cap, and that the Commission approve the use of a 35% load cap per auction.

2. Starting prices

As previously mentioned, in a descending clock auction, prices start high and tick down over time during the course of the auction. Dr. LaCasse explained the "essential elements" of determining starting prices:

> Description: The Auction Manager and Ameren, in consultation with ICC Staff, set a minimum starting price and a maximum starting price for each segment, i.e., separately for the Fixed Pricing Segment under the original rules (the BGS Group of the Fixed Price Section in the rules just discussed) and the Spot Market Segment under the original rules (the BGS Group of the Hourly Price Section in the rules just discussed). Bidders submit indicative offers at the minimum and at the maximum starting prices. The Auction Manager and Ameren, in consultation with ICC Staff, set round 1 prices between the minimum and maximum starting prices.
>
> Purpose: The minimum and maximum starting prices should be set high enough to encourage participation. Competition will tick prices down to their final levels. The range between the minimum and maximum starting prices should be narrow enough to provide bidders with meaningful bounds on the eventual round 1 prices, but wide enough that the actual starting prices will fit within the range even given changes in the market that may occur between the time at which the minimum and maximum starting prices are released and the start of the auction.
>
> Mechanics:
>
> a. The minimum and maximum starting prices will be developed considering recent market data.
>
> b. These market data would include energy forward prices for standard products, capacity market data as available, congestion and wholesale transmission rates.
>
> c. The round 1 prices would take the indicative offer data into account.

(Resp. Ex. 12.0, pp. 85-86, lines 2046-2069)

No party objected to the above-specified description, purpose, and mechanics. Hence, Staff recommends that the Commission approve Ameren's proposal with respect to the auction's starting prices.

3. Bid decrements

As described previously, the SDCA proceeds in biddings rounds, in which suppliers bid quantities in response to the prevailing prices announced by the Auction Manager. In the initial round, the price is set relatively high. Between rounds, the price for each product either ticks down or remains the same. The price ticks down when there is excess supply for that product (i.e., when the total number bids for tranches exceeds the target number of tranches sought for that product). Otherwise (when there is no excess supply for a product), the price remains the same. When there is no longer any excess supply for any of the products, the auction ends. Among the auction rule details is the precise manner in which prices would change between rounds.

In the original proposal, the Ameren Companies did not specify the precise manner in which prices would change between rounds. They indicated that this would be one of the details to be developed by the Auction Manager in consultation with the Staff prior to the auction. However, the fundamental price decrement guidelines that were specified in Dr. LaCasse's testimony implied that bidders might be able to learn much about excess supply for individual products in the auction simply by observing price decrements. Fearing that some bidders might learn too much about excess supply--perhaps providing them with an opportunity to prematurely stop the auction above competitive price levels--Staff witness Salant argued that the detailed price decrement formulas should remain confidential. (ICC Staff Exhibit 1.0, p. 91, lines 2054-2059)

In her rebuttal testimony, Ameren witness LaCasse provided some additional insights about the issue:

> However, I believe it is important to realize that there are limits to how thoroughly this concern can be addressed by this or any other proposal. For the auction to work well, there must be some relationship between the excess supply on a product and the tick down on the product. In fact, the greater is the excess supply on a product, the larger should be the price tick down on that product. It is this principle that ensures that the auction produces prices that are reflective of market. If a price on a product is "too high" compared to the price of another product, bidders can be expected to switch to the product with a higher price, creating excess supply that then drives down the price to a market level.
>
> This principle means that, even if bidders are not provided with the price decrement formulas, bidders will be able to make inferences about the excess supply of each product.

(Resp. Ex. 12.0, p. 90, lines 2141-2152)

Acknowledging the concern that price decrements could provide "too much" excess supply information to bidders, Dr. LaCasse testified that

> I believe that an alternative is to provide bidders with price decrement formulas, but to make sure that these formulas do not allow bidders to make good inferences about the excess supply on a product toward the end of the auction.

(*Id.*, p. 91, lines 2181-2183) Indeed, she presented alternatives (*Id.*, pp. 92-93, lines 2187-2229) that Staff witness Salant supported as "a good structure for setting bid decrements" (ICC Staff Ex. 11.0 Corrected, p. 8, lines 178-179). Dr. Salant also noted that

> I believe that further refinements in the bid decrement formula are advisable, and that there needs to be some decision about parameter values. I support Ameren's proposal for the Auction Manager to work with ICC Staff and the Auction Advisor to fully develop the actual formulas as soon as possible. … Thus, I recommend approval of Ameren's proposal with respect to the bid decrement formula.

(*Id.*, pp. 8-9, lines 179-186) In her surrebuttal testimony, Dr. LaCasse confirmed that

> [T]his is an implementation issue: it is expected that decrement formulas would be finalized closer to the auction, based on final information concerning the number of tranches, bidders in the auction, etc.

(Resp. Ex. 19.0, p. 20, lines 464-467)

In conclusion, price decrements can and should reveal something (but not everything) about the excess supply prevailing at the start of each auction round. Thus, Staff respectfully recommends that the Commission accept this basic principle. Staff also concludes that Ameren witness LaCasse has provided "a good structure for setting bid decrements," but that "it is expected that decrement formulas would be finalized closer to the auction." Thus, Staff recommends that the Commission direct Ameren's Auction Manager to consult with Staff in finalizing those formulas, which would be revealed to bidders prior to the auction in an Auction Manual.

4. Auction volume reductions

An additional "competitive safeguard" advanced by the Ameren Companies is that "The Competitive Procurement Auction Rules filed in this proceeding provide to the Auction Manager the ability to cut back the volume purchased if this is necessary to ensure a competitive bidding environment." (Resp. Ex. 6.0, p. 47, lines 1063-1065) As Ameren witness LaCasse explained,

> For any volume not procured through the auction (for example, any volume cutback from the Fixed Pricing segment by the Auction Manager for purposes of ensuring a competitive result), Ameren's contingency plan specifies that any such volume would be procured through MISO-administered markets. This properly ensures that suppliers do not have

> all opportunity to obtain a contract to serve BGS-FP, BGS-LFP, or BGS-LRTP load outside of their participation in the auction.

(*Id.*, p. 48, lines 1079-1084)

Staff witnesses Salant and Sibley agree that volume cut-backs provide an important safeguard for the reason specified by Dr. LaCasse—insufficient bidder interest in the auction. (see, for example, ICC Staff Exhibit 11.0 Corrected, p. 26) However, Dr. Salant and Professor Sibley go one step further. For example, Professor Sibley states,

> In principle, an auction volume adjustment can completely offset the effect on price due to the exercise of market power by a bidder. A bidder with market power could attempt to "stop the clock" in the auction by reducing the number of tranches bid such that supply equals or falls below demand. As noted above, the anticipated benefit from this strategy is to preserve a high margin on the tranches still bid for. However, a volume adjustment can, by reducing the number of tranches available in the auction, decrease or even eliminate the benefit to a bidder from withholding supply. For example, suppose that when the price falls from $31/MW to $30/MW, a large supplier withdraws sufficient tranches such that the auction manager is tempted to conclude that $30/MW is a competitive price, whereas the true competitive price is $25/MW. The gain to the supplier is the $5 premium multiplied by the number of tranches won. However, if the Auction Manager suspects that the large supplier is attempting to withhold tranches and reduces the auction volume, the number of tranches won by the larger supplier can be reduced to the point where the withholding becomes unprofitable. Knowing this can happen, the large supplier may be deterred from withholding supply.

(ICC Staff Exhibit 2.0 Revised, pp. 18-19, lines 284-300)

Dr. LaCasse took exception to using volume reductions for offsetting the effect on price due to the exercise of market power by a bidder:

> The notion that reducing the volume at auction could mitigate wholesale market power does not seem logical. Reducing the volume procured through auction does not of course reduce the volume that Ameren will ultimately need to procure through the wholesale market to serve its default customers' load. If volume is reduced at the auction, it is procured via MISO wholesale markets. Reducing the auction volume does not mean reducing overall demand.

(Resp. Ex. 12.0, p. 44, lines 1060-1065) Dr. LaCasse made some other noteworthy observations concerning this issue, such as:

> Dr. Salant recommends "some reduction in volume whenever there is precipitous, and what appears premature, withdrawal of tranches, even if this occurs after the first few rounds of the auction" … [T]o the extent that such "precipitous" reduction in volume would reveal a lack of interest in the auction and would mean a bidding environment that is less than competitive, then the principles for the auction volume guidelines already incorporated in the proposed Auction Process are consistent with Dr. Salant's recommendation. Similarly, as I have already testified, the auction volume adjustment guidelines incorporate the possibility for a further adjustment, and this is also consistent with Dr. Salant's recommendation.
>
> …
>
> [A]t the end of the auction, if bidders are estimating a common value opportunity, if bidders have obtained information throughout the auction regarding the excess supply at various price points, if bidders are being squeezed by the auction prices ticking slowly down to their cost, and if the bidding is competitive, it should not be a shock to see several bidders starting to withdraw tranches at similar price points. There is nothing sinister about this. One must remember that the bidders are the experts at assessing the risks of the market and evaluating the opportunity of providing full-requirements service. Seeing several withdrawals as excess supply falls, my first hypothesis would not be strategic price manipulation.
>
> …
>
> Dr. Salant acknowledges that under his proposal, there is a risk of reducing the volume when bids are being withdrawn because "auction prices have fallen below costs." … [B]elieving that the knowledge of one expert, be it the Auction Manager or another party, can best the market knowledge of a group of sophisticated bidders who will have learned from the information provided through the auction process, is froth [sic] with peril. It is also my opinion that should the knowledge of this one expert be used to determine "costs" and should these "costs" be used to punish bidders who withdraw before those "costs" are reached, then the bidders will ask to understand the methodology that is behind the calculation of these costs, and I believe they will be justified in doing so. The actions of the Auction Manager would no longer be simply directed at maintaining a competitive bidding environment in the auction as a whole and for the clear benefit of customers, the actions of the Auction Manager would be responding to the actions of specific bidders who would reasonably expect to understand what they were and were not allowed to do. It is worth

> pointing out that this situation is inherently different from other types of mitigation measures aimed at specific market participants. Mitigation measures typically aim to limit the price obtained by certain market participants to the clear benefit of customers; here, even if the auction prices are somewhat lower because of the volume reduction, the fact that they will be supplemented by spot purchases means that the benefit to customers is less than clear. Finally, enacting this type of principle is putting the auction results at serious risk of challenge from bidders and customers alike – bidders who will want to understand why their actions precipitated the reduction in volume and the customers who will want to understand how such an action would benefit them.

(Resp. Ex. 19.0, pp. 26-27, lines 603-618; p. 30, lines 687-696, pp. 30-31, lines 697-726)

Based on the arguments reviewed above, Staff finds itself persuaded that identification of bidders who are attempting to exercise market power and ***set*** prices—rather than ***respond*** competitively to prices (and excess supply information) called out by the auctioneer—is indeed "fraught with peril." While the proposal by Drs. Salant and Sibley are certainly well-intentioned and theoretically correct, the record unfortunately provides no reliable method for discerning the underlying motivation of suppliers who are withdrawing tranches. Furthermore, even if there were a reliable method for discerning the underlying motivation of suppliers who are withdrawing tranches, Staff is not convinced that volume cutbacks would necessarily be beneficial to ratepayers. As Dr. LaCasse warns, volumes cutbacks are not without risks, since they perforce shift the utilities' demand for energy to some other procurement venue (such as the MISO spot market). Hence, Staff is reluctant to imbue the Auction Manager (or the Staff) with the power to cut back auction volumes, unless it is extremely clear that such reductions will benefit ratepayers. As Dr. LaCasse warns, volumes cutbacks are not without risks, since they perforce shift the utilities' demand for energy to some other procurement venue (such as the MISO spot market).

Thus, Staff respectfully recommends that the Commission accept Dr. LaCasse's position with respect to limitations in the use of volume cutbacks.[5] Staff hastens to add, however, that this recommendation does not affect the right and responsibility of the Staff and the Auction Manager, independently, to address such questions as these (which are excerpted from Resp. Ex. 19.5 "Content of the Confidential Staff Report" that would be given to the Commission at the conclusion of each auction[6]):

- Is there any evidence of collusion or improper coordination among bidders?
- Is there any evidence of a breakdown in competition in the auction?
- Were bidding patterns observed during the auction consistent with competitive bidding and the efficient allocation of load among bidders?

Hence, the Commission (rather than the Auction Manager or Staff) would retain a remedy should it find reason, based on the Auction Manager's Report and/or the Staff Report, to question the competitive integrity of the auction process. The Commission can refuse to certify the results of any auction for any reason, including but not limited to evidence of collusion or improper coordination among bidders or a breakdown in competition. In Staff's view, such a responsibility should rest with the Commission

[5] That being said, Staff also shares Dr. LaCasse's belief "that the gap in Dr. Salant's and my perspectives on the auction volume guidelines is much wider than the gap in our actual recommendations." (Resp. Ex. 19.0, p. 24, lines 559-561) In particular, if the Auction Manager is unable to determine reliably (and in the midst of the auction) if a bidder is strategically attempting to exercise market power and set prices—rather than respond competitively to prices (and excess supply information) called out by the auctioneer—then the Auction Manager certainly cannot launch strategic counter-measures (such as volume cut backs).

[6] Similar questions appear in the Company's proposed Auction Manager Report outline (Resp. Ex. 11.2).

rather than a member of the Commission's Staff or a utility-hired contractor such as an Auction Manager.

Finally, regardless of the resolution of the issues discussed above, both Staff and the Ameren witnesses agree that strict confidentiality should be maintained over the detailed volume reduction guidelines that are yet to be developed. (see, for example, ICC Staff Exhibit 1.0, p. 55; Resp. Ex. 12.0, p. 85; ICC Staff Exhibit 11.0 Corrected, p. 34; and Resp. Ex. 19.0, pp. 24-26) It is important that bidders not be made privy to these detailed guidelines. Furthermore, Staff and the Ameren Companies agree that the Auction Manager and the Staff (with the assistance of any expert auction advisors that Staff may engage) should and will work together to develop those detailed guidelines in compliance with whatever order the Commission should hand down in this docket. For example, during cross examination, Ameren witness LaCasse stated:

> Q. You are not opposed in general to developing auction volume guidelines with Staff as part of the pre auction process, is that correct?
>
> A. That's correct. I would assume that that would be the case.

(Common Tr., p. 936, lines 16-20)

5. Portfolio rebalancing

Staff witness Salant proposed an additional use for auction volume reductions, if and when interest in a particular product within the auction is much lower than interest in other products. (ICC Staff Exhibit 1.0, pp. 59-61) Specifically, he recommended that

> [T]he Auction Manager can reduce auction volume of under-subscribed products and/or shift tranches from more under-subscribed to over-subscribed tranches. … There are several ways in which volumes of different duration tranches can be adjusted during the auction. I

> recommend that the rule followed by the Auction Manager attempt to approximately equalize the ratio of supply to demand across tranches of different durations.

(*Id.*, pp. 59-60, lines 1337-1349)

Ameren witness LaCasse argued that this "portfolio rebalancing" recommendation "should be rejected and that it is likely harmful to the Auction Process," explaining that "bidder interest [in the various products] evolves as the auction progresses," (Resp. Ex. 12.0, p. 59, lines 1406-1410) and that

> The auction is designed so that the relative prices for the various substitute products are discovered through the auction and so that these relative prices track the realities of the market. The judgment of the Auction Manager, even if exercised in accordance with a rule pre-established on the basis of expected bidding patterns, is a poor substitute for this market mechanism. This judgment is even more likely to be misapplied as bidders should be expected to strategically respond to such adjustments, and will devote time and effort to influence the final tranche allocation.

(*Id.*, pp. 59-60, lines 1420-1428)

Dr. Salant, himself, listed other potential disadvantages to portfolio rebalancing. For instance, it could interfere with maintaining a consistent mix of one-year, three-year, and five-year contracts across auctions. In this regard, "the Commission would have to be comfortable relinquishing some of that control to the Auction Manager in consultation with Staff and the Auction Advisor." (ICC Staff Exhibit 11.0 Corrected, p. 55, lines 1260-1269) Despite the drawbacks, he believed that the advantages of portfolio rebalancing could outweigh the disadvantages. (*Id.*, pp. 52-57) Finally, he recommended that the Auction Manager

> should be authorized to utilize the [portfolio rebalancing] option only after consulting with the Staff and there is consensus between the Auction Manager and Staff that such an action is appropriate. The details of how such volume adjustments would be made, like the details of volume adjustments in general, should be a closely guarded confidential

> component of the auction process, to be determined by the Auction Manager in consultation with the Staff and the Auction Advisor prior to the auction.

(*Id.*, p. 56, lines 1276-1282)

In light of the foregoing, Staff respectfully recommends that (1) the Commission authorize Ameren's Auction Manager to utilize the portfolio rebalancing option only after consulting with the Staff and there is consensus between the Auction Manager and Staff that such action is appropriate, provided that (2) Ameren's Auction Manager, in consultation with the Staff and the Auction Advisor, can devise prior to the auction a protocol deemed appropriate by the Auction Manager for carrying out such portfolio rebalancing.

6. Association and confidential information rules

a. The Company's proposed rules

An additional competitive safeguard (in addition to the load caps and provisions for volume cutbacks, discussed above) is the establishment of "association and confidential information rules," which are found in Ameren's proposed "Illinois Auction Rules" (Resp. Ex. 19.3) and its proposed "Part 1 [Bidder] Application Form" (Resp. Ex. 19.1). According to Ameren witness LaCasse,

> The association and confidential information rules are designed specifically for the auction format to ensure that the scope for anti-competitive behavior is minimized. Association and Confidential Information rules have specific measures that ensure the independence of bidders, that ensure that no bidder has information about its competitors' bids, and that ensure that opportunities for coordination among bidders are minimized.

(Resp. Ex. 6.0, p. 46, lines 1034-1039) In Staff's view, such rules are unlikely to ***"ensure"*** independence, but they can at least provide a mechanism for bidders to

assure their independence. Similarly, such rules may not completely "ensure that opportunities for coordination among bidders are minimized," but they may help discourage it.

Staff witness Salant supported such disclosure requirements, in general, testifying,

> Affiliation disclosure requirements are necessary because, absent such provisions, two or more bidders can effectively coordinate bids, and/or a third party can control the bidding of two or more bidders, allowing a single entity to potentially circumvent the load cap.

(ICC Staff Exhibit 1.0, p. 88, lines 1990-1993)

Staff concurs with Dr. LaCasse that there should be an appropriate set of "Association and Confidential Information Rules" within the framework of the proposed auction.

b. Dr. Salant's additional disclosure rules

Dr. Salant also testified that

> Ameren's proposed affiliation disclosure requirements are inadequate because they allow certain types of collusive arrangements to go undetected.
>
> …
>
> To reduce the possibility of arrangements that can circumvent the purpose of the load cap and disclosure provisions, bidders should be required to identify the existence of any contracts they are party to that are contingent on the auction outcome. Bidder reports of such contracts should be only provided to the Auction Manager, the ICC, and the Auction Monitor. (Potential suppliers may decide not to participate in the auction at all unless they can maintain confidentiality of supply agreements they have with third parties.) The Auction Manager can then request that the bidder or the counter party in each contract provide information about whether the counter party has other such contracts.

(ICC Staff Exhibit 1.0, p. 88, lines 1997-1999; p. 89, lines 2016-2025)

Dr. LaCasse rejected Dr. Salant's additional requirement for bidders to reveal their supply contracts, arguing that such a requirement would be unnecessary, would have a chilling effect on participation in the auction due to the competitively sensitive nature such information, and may increase supplier costs as suppliers enter into more complicated contracts to avoid the need to disclose. She concluded, "The ultimate consequence on the auction of one or both of these effects of adding the disclosure requirements is to reduce competition or increase costs to suppliers, both of which can be expected to have a negative effect on price." (Resp. Ex. 12.0, pp. 54-57; quote at Id., p. 57, lines 1363-1366)

Despite these arguments, Dr. Salant maintained the need for the additional disclosure requirements (ICC Staff Exhibit 11.0 Corrected, pp. 36-42), noting, for instance that "a bidder may have no knowledge of any collusive arrangement and may merely be serving as a conduit to implement a collusive arrangement being orchestrated by an upstream supplier." (Id., p. 39, lines 880-883) To clarify his proposal, Dr. Salant indicated that bidders would only have to disclose information concerning full-requirements contracts with their suppliers. The Auction Manager, utilizing these additional disclosures,

> should then ascertain whether the affiliated bidders would, in aggregate, exceed the load cap and, if so, ask them to restructure their agreements, reduce eligibility or otherwise modify their agreements to stay under the load cap. While these affiliation disclosure requirements may involve disclosure of sensitive business information, I have tried to structure the disclosure requirements to only uncover situations in which the contract terms themselves implicitly dictate bidding strategy.

(*Id.*, p. 42, lines 947-953)

In surrebuttal testimony, Dr. LaCasse responded, "The clarification of Dr. Salant's position only makes me believe more strongly that his recommendations on contract disclosures are not well founded, have no benefits, and certainly can be harmful to the auction." (Resp. Ex. 19.0, p. 37, lines 846-848) For instance, with respect to the claim that Dr. Salant's proposal is not well founded and would have no benefits, she noted,

> I do not deny that the upstream supplier will have information concerning the bidding strategy of the bidders it supplies by virtue of having contracted with them. I do not deny that the auction price emerges as bidders bid on the basis of their supply arrangements coming into the auction (should they have any) and this is true in particular if a bidder holds a full-requirements contract. But that is a long way from an upstream supplier determining or exerting direct influence over the auction price.

(*Id.*, p. 40, lines 916-923)

With respect to how Dr. Salant's clarified proposal could be harmful, she noted that a bidder could have lined up supply, all-the-while being very careful top avoid contravening the Association and Confidential Association rules, but then,

> After submitting the Part 2 Application, the bidder gets a call from the Auction Manager. The bidder learns that it must reduce the amount it is bidding in the auction, or it must agree not to participate, or it must agree not to use the full-requirements deal to support its bid and go instead to another source of supply that it had determined was s higher cost. This is through no fault of its own: short of dismissing out of hand the option of taking a full-requirements contract from any upstream supplier at the very beginning of the process, there is nothing the bidder could have done in its preparation for the auction to avoid this situation or to ensure that its costly preparations for the auction were not made in vain. The bidder is penalized and must re-organize its bid while having taken all possible actions to conform to the Association and Confidentiality Information Rules and all other requirements of the Auction Process. … Furthermore, once the Auction Manager tells bidders to re-organize, abandon their supply contracts, or reduce their participation, the Auction Manager has now revealed to those bidders information that they were prohibited by the Association and Confidential Information Rules from revealing themselves. The bidders have now learned that 1) other bidders also have full-requirements contract with the same upstream supplier and 2) the indicative offers of all such bidders after they comply with the requirement to re-organize will be precisely equal to the load cap. … The Auction Manager has now given these affected bidders some highly confidential information that other bidders will not have, and that provide affected

bidders with tools to attempt to implement a collusive agreements if they so wish.

(*Id.*, pp. 45-47, lines 1040-1077)

That is, Dr. LaCasse expects that Dr. Salant's proposal might lead to more disclosure of bidders' confidential information not just to the Auction Manager, but to other bidders, as well. Ironically, the potential for collusion would increase rather than decrease.

In conclusion, Staff recognizes that there are reasonable arguments against requiring additional disclosure of full-requirements contract information. Thus, considering the real potential for some negative unintended consequences, Staff does not recommend at this time that the Commission order Ameren to modify the association and confidential information rules.

7. Tranche size

In the proposed auction, bidders vie to supply one or more "tranches" of one or more of the sought-after products. As already noted, the size of each tranche is ultimately expressed, contractually, as a percentage of the customer segment's full-requirements load at any and all times during the life of the contract. However, to put the percentage into perspective, the Ameren Companies also expressed this as an approximate number of megawatts ("MW") of the customer segment's peak load. In its original filing, the Ameren Companies proposed that each tranche should be approximately 100 MW. (Resp. Ex. 6.0, p. 81, lines 1824-1825)

In his direct testimony, Staff witness Salant argued that the tranche size should be significantly smaller than 100 MW at peak, in order to accommodate smaller suppliers or even large suppliers that wish to supply odd lot sizes. (ICC Staff Exhibit 1.0, pp. 55-58) He recommended an approximate tranche size of 5 MW. (ICC Staff Exhibit 1.0, p. 58, lines 1297-1302) No other party expressed any concerns about tranche size.

In its rebuttal testimony, Ameren reduced its proposed tranche size to 50 MW, in response to Staff's concerns. (Resp. Ex. 12.0, pp. 53-54) Staff witness Salant accepted this compromise, concluding that "Ameren's revised proposal [is] a reasonable one at this time and I recommend the approval of a 50 MW tranche size for Ameren's first auction." (ICC Staff Exhibit 11.0 Corrected, p. 16, lines 346-347) No other parties took issue with the proposal. Hence, Staff respectfully recommends that the Commission approve the revised proposal to define tranche size as approximately 50 MW of each customer segment's peak demand.

8. "Price taker" proposal

In conjunction with his recommendation to reduce the load cap from 50 percent to somewhere in the range of 25-35 percent (discussed in subsection 1, above), Staff witness Salant also proposed an innovative addition to the Ameren Companies' auction proposal: a "price taker" option. As summarized by Dr. Salant,

> One way to have lower load caps while allowing large suppliers to participate fully in the Illinois CPP is to require suppliers who wish to exceed the load cap to commit to accepting the final auction price prior to the auction.
>
> [But since] one function of load caps is to limit Ameren's and Illinois ratepayers' exposure to any one particular supplier, and thus to limit the credit risk borne by Ameren and Illinois ratepayers, … no price-taking supplier would be allowed to supply more than 50 percent of the tranches for each utility."

(ICC Staff Exhibit 1.0, pp. 70-71, lines 1595-1598; pp. 71-72, lines 1612-1615 and 1623-1625)

Dr. Salant further explained how the price-taker option would be integrated into the auction scheme:

> Meanwhile, the auction price will be determined by competition among suppliers in the auction, but the lower load cap for active bidders in my proposal implies that large suppliers will have less of an effect on the determination of the auction price than they would under Ameren's proposed 50 percent load cap. Thus, my proposal reduces the market power that can be exercised by any one firm, while still allowing large suppliers to potentially supply up to 50 percent of the tranches in an auction. The increased competitiveness of the auction can be expected to lead to lower final auction prices.

(*Id.*, p. 74, lines 1668-1676)

Finally, explaining why a supplier may wish to opt for the price-taker option, Dr. Salant opined:

> When a large supplier expects that the auction price will exceed its marginal costs, then that supplier would prefer to produce up to its capacity, and hence would choose to commit it to an amount of supply up to its capacity prior to the auction. If a large supplier expects the auction price to be either close to or lower than that supplier's marginal costs, then that supplier would prefer not to commit supply prior to the auction, and will drop out of the auction once the price falls below its marginal cost. However, since the large suppliers are likely also the low-cost suppliers in Illinois, it is likely that the final auction price will exceed a large supplier's marginal costs. For this reason, a large supplier may be willing to commit to supplying all or most of its capacity in advance of the auction.

(*Id.*, p. 73, lines 1652-1662)

In response to Dr. Salant's price-taker proposal, Ameren witness LaCasse charged that

> The logic underlying the proposal, that a large bidder has low marginal costs and will be willing to be a price taker if it expects the auction price to be high enough, is flawed and confuses competition in the auction and competition in the wholesale market. Dr. Salant assumes that large bidders are also likely to be those with low marginal production costs. He

> reasons that as a result these bidders would be willing to be price takers as the auction price will almost surely exceed their marginal costs. This analysis is incorrect. The point he misses is that the marginal cost of generation is not the marginal cost of auction participation. The true marginal cost of participating in the auction is the opportunity cost of selling in the auction. The opportunity cost of selling in the auction is the revenue foregone of the next best opportunity, most likely the opportunity of selling forward power products elsewhere, including in wholesale markets or to other auction participants. … Dr. Salant's misconception of the auction product is also evident in his response to ComEd Data Request Staff 2.40 in Docket 05-0159. When asked what is an inefficiently high auction price, Dr. Salant responded: "A price is inefficiently high if it is above the marginal cost of the marginal unit." While the notion that electricity prices should be based on the marginal cost of the marginal unit underlies much of the theory of price formation in competitive wholesale spot power markets, it is not the notion that is relevant to the auction product.

(Resp. Ex. 12.0, pp. 46-47, lines 1103-1126)

Staff accepts Dr. LaCasse's criticism, to a point. However, while Dr. LaCasse is correct to identify distinctions between competition in the auction and competition in the wholesale markets, as well as distinctions between auction products and wholesale market products, Dr. LaCasse goes too far when, because of these distinctions, she seems to conclude there is no connection between the cost structures of major generating firms operating in the wholesale markets and the way in which such firms will bid in the auction. (ICC Staff Exhibit 11.0 Corrected, p. 61, lines 1397-1403) Dr. Salant agreed that the opportunity cost of selling in the auction is the revenue foregone of the next best opportunity, and that therefore, the marginal cost of supplying the auction product is not the marginal cost of production of a generation unit. (*Id.*, pp. 61-62, lines 1408-1430) However, Dr. LaCasse apparently fails to recognize that the "next best opportunity" for one firm may not be exactly the same as the "next best opportunity" for the other firms bidding in the auction. (*Id.*, p. 62) That is, bidders having ***very similar*** opportunity costs (as Dr. Salant seems to expect) is not the same thing, and not as extreme, as bidders having ***absolutely identical*** opportunity costs (as Dr. LaCasse insists).

However, Dr. LaCasse testified about several additional ways in which the proposal could be harmful, including:

> First, … In the extreme circumstance in which several suppliers come forward to be price-takers, the volume at the auction [according to Dr. Salant's proposal] will be the greater of 10% of tranches available or 1 tranche. I would submit that many suppliers will not want to incur the costs of participating in the auction for such a low volume. (How many suppliers could Dr. Salant really expect to show up to compete for 1 tranche?) The price of these tranches – and therefore the price for the entire load and to be paid by all customers – will not be set by the full pool of suppliers that would have otherwise competed in the auction. A price will be obtained at the auction, but it is unlikely to be either competitive or to be a market price. These considerations will still come to bear, albeit to a lesser extent, if there is a single price-taker, who could request up to 50% of the load. … The price at auction will certainly not reflect the full competition of all bidders that we would have expected to participate and there is no reason to suspect let alone believe that the price from the competition of a smaller pool of bidders would be lower.
>
> Second, I believe the price-taking option is likely to deter participation in the Auction Process. Bidders may not be willing to invest resources and prepare their bids with the possibility that, at the end of the day, they will be competing for a small auction volume. Furthermore, any benefit of the load cap in terms of maximizing the participation of suppliers, especially smaller suppliers, is lost if a price-taking option is introduced. The load cap reassures smaller or newer suppliers that each and every bidder would be limited in its ability to bid and win load, and that these smaller suppliers would be free to complete with all bidders including those that they may be perceived to be more established suppliers. A price-taking option gives the option to a supplier of reserving a portion of the supply for itself without having to compete for it. Smaller or newer suppliers may well perceive the price-taking option as a barrier that prevents them from competing with more established players on an equal basis for all the load. Knowing that such an option exists may well discourage the participation of these suppliers.
>
> Third, I believe that the price-taking option negates many of the benefits of the open auction format. The benefits of the clock auction are based on bidders being able to use information that they obtain during the Auction Process to revise their bids, and this dynamic information feedback tends to elicit the best bids. The price-taking option negates these benefits in

> two ways. The proposal effectively forces the price-taker to bid as it would in a sealed bid situation, and deprives customers of the better bids that could result if the large bidder had the information provided through the open auction format. By the same token, the existence of a price taker denies information to suppliers that actually participate in the auction as well. They would not see market supply at different price points; the supply from the price-taker is fixed at all price points and does not provide information. This could well lead to less aggressive bids as the bidders would be less confident of the information that they learn during the auction from others' willingness to supply.

(Resp. Ex. 12.0, pp. 47-48, lines 1137-1158; p. 49, lines 1162-1176; pp. 49-50, lines 1177-1190) While Dr. Salant replied to most of these points in rebuttal testimony, Dr. LaCasse correctly observes that

> Dr. Salant does not rebut many of the points that make the price-taker proposal impractical and harmful to the process as explained in my rebuttal testimony. Dr. Salant does not rebut the point that the price-taker option negates the advantages of the open auction, that the price-taker option means that the auction price is potentially no longer a market based price, and that there are practical problems apportioning the indicative offers, especially for multiple price-takers, across the various products to ensure that all are subject to the discipline of bidding from the auction.

(Resp. Ex. 19.0, p. 52, lines 1196-1203)

In Staff's view, the price taker option is unlikely to have much of an effect on the auction, either a positive or a negative effect. Hence, Staff is largely ambivalent the proposal, at this time. Furthermore, since suppliers can also sell their power to other bidders or into the MISO organized markets, or in other bilateral markets, the price taker option is not necessary for consumers to gain access to low-cost producers' power. Thus, at this time, Staff does not recommend that the Commission order Ameren to incorporate the price taker option into the auction.

9. Other format concepts and issues

Staff has nothing to add at this time, but reserves the right to respond in its reply brief to parties who introduce other format concepts and issues in their initial briefs.

D. Clearing price: uniform vs. pay-as-bid

The Ameren Companies' proposed SDCA would result in a uniform auction clearing price for each product. AG witness Reny also discussed a type of auction utilizing "price caps, possibly distinct price caps for distinct suppliers." Presumably, then, Dr. Reny's alternative auction format might result in non-uniform clearing prices.

AG witness Reny dismissed the Ameren Companies' uniform-price approach "because the auction does not specify a price cap (sometimes also called a reserve price) for any of the suppliers." (AG Ex. 4.0, p. 3, lines 18-19) He further explained,

> A well-established result in the auction literature is that a buyer can expect a lower price to result from a procurement auction among suppliers when he sets an appropriate price cap. A price cap limits the extent to which a supplier can overstate its cost. In effect, a price cap acts as an additional competitive bid which suppliers must improve upon in order to win the contract. Further, when different suppliers have different costs, setting lower price caps for suppliers with lower expected costs can reduce the expected price even more.

(*Id.*, p. 3, line 19 - p. 4, line 4)

Dr. Reny went on to argue that

> [A]n auction with appropriate price caps can yield lower prices than either a pay-as-bid or uniform-price auction. Alternatively, a multilateral negotiation can also yield lower prices than either a pay-as-bid or uniform-price auction. A multilateral negotiation can take many forms. However, it typically differs from a procurement auction in that the buyer engages in bargaining, making offers and counteroffers with the suppliers. The buyer is therefore directly involved in the price formation process, unlike in an auction where the suppliers alone determine the price. The reason a multilateral negotiation might yield a lower price than either a pay-as-bid or

> uniform-price auction is that direct participation allows a shrewd buyer to implement price caps by holding firm and refusing to purchase from suppliers at prices above which the buyer expects they can afford to accept.

(*Id*., p. 4, lines 7-19)

Dr. Reny explained that the benefits for the buyer of using a multilateral negotiation rather than an auction depend on certain circumstances, namely: (i) the suppliers' costs are significantly different; (ii) reasonably accurate information about each supplier's cost is available; (iii) the auction fails to specify a price cap for any supplier; (iv) the buyer is a large purchaser with enough buying power that no single supplier has substantial bargaining power relative to the buyer. (*Id.*, p. 4, line 22-p. 5, line 6) However, "[a] well-designed auction that includes price caps, possibly distinct price caps for distinct suppliers, can achieve prices as low as, and perhaps even lower than, prices obtained through multilateral negotiations. (*Id.*, p. 5, lines 18-21)

Since the AG did not present Dr. Reny's testimony until the rebuttal stage in the proceeding, no Staff witness had an opportunity to respond to Dr. Reny's ideas. However, in surrebuttal testimony, Ameren witness LaCasse responded to Dr. Reny. For instance, Dr. LaCasse addressed the conditions necessary for Dr. Reny's approach to succeed:

> In my opinion, it does not seem likely that all these conditions would hold. For example, I believe that reasonably accurate information about each supplier's cost of providing full requirements service is unlikely to be available. Furthermore, although I discuss in Section 5 of this testimony Ameren's "buying power", i.e., the manner in which Ameren can leverage its ability to buy all load in a single auction, this does not necessarily mean that there would be an absence of any bargaining power on the other side of the market. Finally, I would expect that suppliers' costs could more accurately be described as closely clustered than widely disparate. A supplier's costs in the auction are really their opportunity cost of participation. Although all bidders do not face the same exact opportunity

> costs, they are all evaluating a common market opportunity on the basis of a common forward market.

(Resp. Ex. 19.0, pp. 82-83, lines1907-1918)

Based on these and other considerations (*Id*., pp. 78-84), Dr. LaCasse finally concluded:

> Professor Reny provides highly theoretical testimony that is basically of the “anything’s possible” nature. He provides no proposal, no recommendation or no definite opinion that the two general items that he describes – bidder-specific price caps and multilateral negotiations – are in fact superior to the proposed Auction Process, to each other, or to any other procurement method. He does not relate his musings to the actual market in question. He does not relate his ideas to the multiple goals of the procurement process nor does he address practical issues such as cost recovery approvals. His testimony provides no plausible basis to suspect that the broad and unspecified ideas he discusses would be beneficial to customers or should be considered further, let alone any basis to actually incorporate these concepts into the proposed Auction Process.

(*Id*., p. 84, lines 1947-1957)

Staff agrees with Dr. LaCasse’s assessment of Dr. Reny’s testimony. Dr. Reny fails (1) to relate his theories to the actual market in question, (2) to address practical issues, and (3) to provide a workable alternative for the Commission to consider in this docket. Furthermore, Dr. Reny’s testimony does not provide a concrete basis for rejecting the Ameren Companies’ SDCA proposal.

E. Auction management

1. Auction manager

Ameren witness Nelson testified that

> The proposed CPA process is modeled after the New Jersey auction process designed, in large part, by Dr. LaCasse, who is expected to act as the independent Auction Manager.

…

> [T]he auction has been designed and will be administered by an independent Auction Manager. We will neither run the auction nor determine the winning suppliers. In addition, the auction will be conducted under the supervision of the Staff and an independent Auction Advisor. Thus, our proposal will clearly and fully meet the oversight principle and the other requirements set forth by FERC.

(Resp. Ex. 2.0 Corrected, p. 19, lines 400-402; p. 47, lines 1060-1065)

Staff has reviewed Dr. LaCasse's qualifications (Resp. Ex. 6.0, pp. 1-8) and is satisfied that she is competent to be the Auction Manager for this competitive procurement process. In addition, Staff expects that whoever is chosen as Auction Manager would share a desire by the Ameren Companies to have an auction that runs smoothly and results in as many tranches being filled as possible.

However, Staff does have concerns over the ***independence*** of whomever ComEd and the Ameren Companies hire as the Auction Manager. This concern arises primarily because both ComEd and the Ameren Companies have affiliates who are engaged in the sale of wholesale power and who could be bidders in the proposed auctions. This concern can be explained as follows.

Generally speaking, Staff believes that retail consumers want ***low prices***, along with price stability and service reliability. These are the goals that the Staff would want the Auction Manager to embrace, wholeheartedly, and without reservation. According to Ameren witness Warner Baxter (Executive Vice President and Chief Financial Officer of Ameren): this seems to be Ameren's intent, as well:

> [T]he proposed auction process is open, transparent, fair and designed to procure power at least-cost, while promoting price stability and minimizing volatility. It satisfies federal and state standards and preserves the Commission's authority over power procurement. As we also explain in our testimony, the auction process was selected after long consideration and the involvement of numerous stakeholders.

> …
>
> What we have proposed is a model that we know has worked elsewhere and that is designed to get the best price from the market for our customers.

(Resp. Ex. 1.0, p. 4, lines 53-58; p. 8, lines 151-152)

However, the Ameren Companies propose a "pass-through" of procurement costs (i.e., a cost-tracking mechanism, whereby the Ameren Companies' experience neither gains nor losses on retail sales of electricity). Hence, while the Companies arguably have no disincentive to obtain low prices, by the same argument, they may have little to no incentive to do so, either.

In contrast, the Ameren Companies' wholesale power generating and marketing affiliates (and hence, the Ameren holding company) cannot be expected to be in favor of or indifferent toward low prices; rather, they can be expected to desire ***high*** prices. Herein lies the crux of the problem. The fact that the Ameren Companies are owned by Ameren Corporation, and Ameren Corporation would profit from ***higher*** rather than lower auction prices (all else constant), creates a tremendous conflict of interest for both the Ameren Companies (as electricity purchasing agents for ratepayers) and the "independent" Auction Manager. The Auction Manager is effectively working for two sets of bosses: one (the utilities) that have no particularly strong incentives but at least a duty to get low prices for retail customers; and another (the Ameren holding company) that has an incentive to get high prices for its generation and marketing affiliates participating in the auction.

To avoid such conflicts of interest, Staff witness Salant recommended that "a neutral party should be appointed by the ICC as the Auction Manager for the Illinois CPP." (ICC Staff Exhibit 1.0, p. 94, lines 2123-2125) However, in the event that an independent Auction Manager is not appointed, Dr. Salant recommended that the Commission should

> … limit the discretion of the Auction Manager on any decision that could affect bidders that are affiliated with Ameren differently than bidders that are not affiliated with Ameren. …
>
> In addition, I recommend that the ICC and the Auction Monitor review the actions taken by the Auction Manager prior to the auction based on pre-defined guidelines. For example, the application and credit review can be performed by the Auction Manager, who can then provide a report to the ICC for its review and approval. Such a process will facilitate greater accountability on the part of the Auction Manager.

(*Id.*, lines 2130-2132 and 2134-2139)

In rebuttal testimony, Ameren witness Nelson explained how the Ameren Companies were supporting proposals to reinforce the independence of the Auction Manager:

> We have considered the proposals to reinforce further the existing independence of the Auction Manager made primarily by Staff. While the Ameren Companies believe that their original proposal accomplished that goal, we strongly support the transparency and fairness of the auction, in fact and appearance, and therefore have no objection to reasonable proposals to reinforce that independence, while still respecting utilities' legitimate special role as the purchaser. To this end, the Ameren Companies would agree it is reasonable for the Commission to direct that: (1) the Auction Manager should conduct the auction in close consultation with Commission Staff, and that decisions made by the exercise of the Auction Manager's professional judgment during the auction will be made in consultation with a Staff lead designated by the Manager of the Energy Division; (2) representatives of the Ameren Companies not be present "in the room" during the actual conduct of the auction, not be permitted to direct or influence the Auction Manager's conduct of the action, and not be permitted to communicate with the Auction Manager during the running of the auction; and (3) the Ameren Companies will be entitled to round by round data concerning the price and excess aggregate supply for each product and term, provided that this information will only be shared with specific persons at the Ameren Companies who will be identified by name to the Manager of the Energy Division in advance. The Ameren Companies are also committed to continuing to define the auction process so the rules of the e auction and the criteria by which bidders' actions are to be reviewed are known well before the auction begins.

(Resp. Ex. 10.0 Corrected, pp. 4-5, lines 75-96)

Dr. LaCasse addressed Dr. Salant's concerns about the Auction Manager's discretion in some detail. (Resp. Ex. 12.0, pp. 93-100) With respect to Dr. Salant's call for a review of actions taken by the Auction Manager, Dr. LaCasse summarized--in Resp. Exhibit 12.6--the involvement of the ICC Staff and its auction advisor(s) in the entire auction process. In her discussion of Resp. Exhibit 12.6, she testified,

> This exhibit presents the major events and decision points of the Auction Process, from the time at which final documents have been provided to bidders to the end of the Auction. This exhibit illustrates that the crucial steps of the Auction Process are administered by the Auction Manager in collaboration with the ICC Staff, with the assistance of their Auction Advisor as needed. This exhibit also illustrates that although Ameren participates in the process by providing information and data to the Auction Manager, making assessments related to credit and the administration of the Supplier Forward Contracts, Ameren does not direct or even participate in the major decisions and activities of the Auction Process. In particular, the Auction Manager and the ICC Staff with the assistance of their Advisor, who will all monitor the bids during the Auction and administer the bidding process, will have no contact with Ameren during the auction.

(Resp. Ex. 12.0, p. 102, lines 2456-2468)

In his rebuttal testimony, Dr. Salant assessed the above-mentioned replies by the Ameren Companies and concluded

> Ameren has recognized the need for measures to ensure the independence of the Auction Manager. In its revised proposal, Ameren has supported the adoption of some measures to mitigate potential conflicts of interest. … Thus, I recommend approval of Ameren's revised proposal with respect to the Auction Manager's role and requirements to coordinate with ICC Staff and the Auction Advisor, subject to my recommendations in Section IV below.

(ICC Staff Exhibit 11.0 Corrected, p. 24, lines 542-552 (citations omitted))

Staff has struggled with the Auction Manager independence issue since the inception of this docket. Staff believes that there are pros and cons to the Commission having direct control over the Auction Manager. On the one hand, Staff is highly sensitive to the conflict of interest that arises between ratepayers (represented by their purchasing agent, the Ameren Companies), and Ameren Corporation's generating and marketing affiliates. Given such conflict, whose interests are the Auction Manager expected to hold supreme?

One the other hand, one cannot deny that the Ameren Companies, as public utilities, ***are*** the purchasing agents for their retail customers. Ameren witness Nelson testified that the utilities have a "legitimate special role as the purchaser." (Resp. Ex. 10.0 Corrected, p. 4, lines 80-81) The Ameren Companies have the resources and the responsibility to obtain power at least-cost and provide service at just and reasonable rates. It is not the Commission's role to take over or to micro manage public utility functions.

In addition, Staff notes that the conflict of interest problem identified above is not avoided merely by adopting a different procurement process. The same type of conflict would exist if the Ameren Companies, instead of using a vertical tranche auction, were using any other procurement approach that allows affiliate contracts. Indeed, part of the appeal of the vertical tranche auction approach is that it can help regulators manage the conflict of interest problem. As Staff witness Zuraski pointed out in his rebuttal testimony,

> In terms of dealing with market power and affiliate abuse concerns, the transparency of the vertical tranche auction is its central strength. This transparency is provided by the uniformity of the auctioned vertical tranche full requirement product as well as the bidding mechanism of the auction. Relative to requests for proposal (which are bilateral processes traditionally used in the Midwest for the procurement of electricity), an auction for a uniform product increases the comparability of offers. The comparability of the offers, in turn, increases competition among suppliers

> and provides transparency to the process. Suppliers are, in the end, evaluated solely on the price upon which they can supply a pre-defined product. Since all potential suppliers are ultimately judged on the same observable criterion, this minimizes the potential for utilities to provide favorable treatment to their affiliates, and reduces the burden of regulatory oversight. The bidding mechanism also provides a means for bidders to have their bids considered objectively, fairly, and simultaneously, further adding to the transparency to the process.

(excerpt from page 12 of "The Post-2006 Initiative: Final Staff Report to the Commission," released in November 2004, quoted in ICC Staff Exhibit 12.0, p. 5)

Thus, for all the reasons discussed above, including the fact that Staff will be able to monitor and provide input on the various Auction Manager functions, Staff respectfully recommends that the Commission approve the Ameren Companies' proposal to hire an independent Auction Manager.

2. Role of Ameren

As described in sub-section E.1, above, Staff believes that the Ameren Companies (as electricity purchasing agents for retail ratepayers), have a conflict of interest due to their affiliation with Ameren Corporation's generating and power marketing subsidiaries. This conflict was underscored during cross examination of at least two Ameren witnesses, who revealed that they were receiving significant levels of executive compensation in the form of Ameren Corporation stock options or other Ameren securities: Mr. Nelson, Vice President for Strategic Initiatives of Ameren Services Company and Vice President of AmerenCIPS (Tr., pp. 118-120); and Warner L. Baxter, Executive Vice President and Chief Financial Officer for Ameren Corporation (Tr., pp. 409-415; and AG Cross Exhibits 16, 17, and 18). According to AG Cross Exhibit 17, as of the middle of February 2005, Mr. Baxter owned 1,593 shares of

Ameren Corporation stock indirectly (in his 401-K plan) and an additional 29,991 shares directly, for a total of 31,584 common shares, worth over $1.5 million on February 15, 2005, when the stock price was approximately $51.6 per share. In addition to having a significant personal financial interest in Ameren Corporation, Mr. Baxter also indicated that he is an officer, not only of AmerenCILCO, AmerenCIPS and AmerenIP, but also of Ameren Corporation and Ameren Generating Company; and, as an officer of those companies, his "duties to the shareholders are to earn them a fair return on their investments among other things." (Tr., pp. 421-423; quote at 423)

With its senior policy makers and decision makers having responsibilities for the Ameren Companies as well as Ameren Generating Company, and with their own financial well-being tied directly to the overall Ameren Corporation, Staff is very concerned about the conflict of interest facing them with respect to using the proposed auction to obtain low prices for ratepayers. However, the Ameren Companies have made a significant concession that addresses the conflict of interest issue. Specifically, they have agreed that

> … representatives of the Ameren Companies not be present "in the room" during the actual conduct of the auction, not be permitted to direct or influence the Auction Manager's conduct of the action, and not be permitted to communicate with the Auction Manager during the running of the auction…

(Resp. Ex. 10.0 Corrected, p. 4, lines 86-89)

With this restriction—along with the measures described in sub-section E.1 to limit the discretion of the Ameren-employed Auction Manager and to reinforce the independence of the Auction Manager—Staff believes that the role of the Ameren Companies in the auction have been satisfactorily narrowed to minimize undue influence over the auction, notwithstanding the conflict of interest problem with which the Commission has been confronted in this case. Furthermore, Staff believes that the Commission has relatively wide latitude to prescribe the form of the auction and any safeguards deemed warranted, provided such dictates are consistent with the record evidence and governing laws.

3. Role of Staff

Given all the discussion in sub-sections 1 and 2, above, Staff believes that the Staff, as an agent for the Commission, should play a definite role in the implementation of any auction approved in this docket. For its own part, "the Ameren Companies would agree it is reasonable for the Commission to direct that … the Auction Manager should conduct the auction in close consultation with Commission Staff, and that decisions made by the exercise of the Auction Manager's professional judgment during the auction will be made in consultation with a Staff lead designated by the Manager of the Energy Division." (Resp. Ex. 10.0 Corrected, p. 4, lines 81-86) In addition, "the Ameren Companies now propose that the monitoring, reporting and other activities previously proposed for the Auction Advisor be performed by the ICC Staff in consultation with the Auction Advisor and/or any other expert(s) the ICC Staff believes would be appropriate" (Resp. Ex. 11.0 (Revised), p. 53, lines 1189-1193) As Ameren witness Blessing explained,

> To properly monitor, report, and perform other activities relative to the auction review, the responsible party should have: (a) a deep and broad experience in Illinois and expertise with Illinois-specific issues – for example, administration of the Public Utilities Act; and (b) technical auction experience. The ICC Staff has the necessary Illinois background and is best suited to bring together the technical knowledge of the Auction Advisor and other technical experts. Based on its reconsideration of these factors, the Ameren Companies now believe that the Illinois consumers

> will be best protected by the ICC Staff taking a principal role in the auction review.

(*Id.*, p. 54, lines 1196-1204) Mr. Blessing also proposed what he believed would be an appropriate outline for a Staff Report to the Commission following each auction (within one business day), which he described as follows:

> The Ameren Companies anticipate that the report would address four general areas: (a) pre-auction activities; (b) the conduct of the auction; (c) external events that may have affected the auction results; and (d) any issues, concerns or recommendations identified by the ICC Staff.

(*Id.*, p. 56, lines, lines 1244-1247)

Staff witness Zuraski concurred with this proposed role for the Staff in observing and assessing the auction. Staff witness Salant, while proposing some minor modifications to Mr. Blessing's suggested Staff Report outline, agreed that "Respondent Exhibit 11.2 provides a good starting place for defining the contents of the Staff Report that will be made available the day following the auction conclusion." (ICC Staff Exhibit 11.0 Corrected, p. 48, lines 1093-1095) The Ameren Companies then provided a revised set of suggestions for the Staff Report outline with its surrebuttal testimony. (Resp. Ex. 19.5) As will be discussed in the sub-section entitled, "Regulatory oversight and review," below, Staff believes that the details of the Staff Report outline have been adequately resolved.

4. Representation of consumer interests / separate consumer observer

CUB witness Steinhurst made the following recommendation:

> I recommend that the Commission provide a role for Consumer Observer. This role would be similar to that of the Auction Advisor proposed by

Ameren who would be charged with observing and reporting on how well the process conforms to the approved model.

(CUB Exhibit 2.0, p. 20, lines 454-457)

Explaining the proposal in greater detail, Dr. Steinhurst added,

The Consumer Observer's role is multi-faceted. It includes the following activities:

a. Observing all activities leading up to the auction itself, including software development and testing, bidder education and communications, bidder qualification, and so on;

b. Observing preparatory steps such as establishment of the opening prices and number of tranches;

c. Real-time monitoring of all aspects of the auction;

d. Reviewing and analyzing auction data and documents, as needed;

e. Briefing of the Commission Staff on all of the above;

f. Forming its own assessment of the auction;

g. Making recommendations to the Commission regarding the acceptance or rejection of the auction results;

h. Assisting the Commission in its decision on acceptance or rejection of the auction;

i. Providing an independent report covering the same issues and factors as do the Auction Manager's and Auction Advisor's reports to the Commission;

j. Making recommendations to the commission about future auctions.

…

The consumer observer should be selected by, and only by, the specific consumer advocacy entities that are identified as appropriate for that role in the design of the auction procurement.

…

The entities that appoint the Consumer Observer and to whom the Consumer Observer reports and is accountable should be recognized as official consumer advocates. Possible choices include the Citizens Utility

> Board (CUB) and the Illinois Attorney General's Office. There may be similar entities in other regions of the state. Ad hoc membership organizations, such as representatives of only limited subsets of consumers, should not be included. Whatever entities are included should be subject to the jurisdiction of the Commission, at least for the purpose of enforcement of the agreements or orders governing the activities of the Consumer Observer.

(*Id.*, pp. 22-23, lines 500-517; p. 24, lines 549-551; p. 25, lines 559-567)

In response to Dr. Steinhurst's Consumer Observer proposal, Ameren witness Nelson stated,

> The Ameren Companies believe that the ICC Staff can protect the interests of consumers in a fairly run and effective auction. That said, the Ameren Companies remain open to the participation of a consumer representative on appropriate terms. Those terms, at a minimum, would have to address the confidentiality concerns I have described above. I would also note that, while the Ameren Companies are not objecting to the idea of a consumer representative, CUB's proposal also clears the way for other interested parties to seek their own private auction observers. Giving each party to this case its own auction representative is administratively unworkable, would require broad distribution of confidential material, and would harm the auction process.

(Resp. Ex. 10.0 Corrected, p. 22, lines 507-516)

While Staff is willing to accept the responsibility for observing and assessing the auction as a neutral party, which Staff believes is in the best interest of consumers, Staff takes no position with respect to the CUB proposal for an additional "Consumer Observer."

F. Date of initial auction

The Ameren Companies initially proposed the month of May 2006 as the timeframe for the initial auction. (ICC Staff Exhibit 5.0, p. 18, line 396) CES and CCG agreed with the Ameren Companies' proposed timeframe for the auction. (CES Ex. 1.0,

p. 10, lines 206-208; CCG Exhibit 1.0, p. 5, lines 123-125) The Companies indicated that their May 2006 proposal was based on many factors, including (a) its desire to avoid the more volatile summer and winter months; (b) proximity of the auction date to the delivery period; and (c) input from suppliers. (Resp. Ex. 10.0 Corrected, p. 14, lines 307-310)

In support of a May 2006 date, CES reasoned that an auction scheduled for May 2006 could be delayed until September 2006 to allow time for the Auction Manager to address problems that may arise. (CES Ex. 1.0, p. 11, lines 231-235; CES Ex. 2.0, p. 4, lines 61-62) CCG witness Smith stated that May 2006 would allow sufficient time for winning bidders to hedge their positions prior to the delivery date of January 2007. (CCG Exhibit 1.0. p. 5, lines 125-127)

Staff originally recommended July 2006 as the date for the initial auction. Staff argued that, since the 2006 auctions would be the first of their kind in Illinois, it would be wise to ensure that an adequate amount of preparation could occur before the auction takes place. In this regard, the date of July 2006 would provide two additional months of preparation time over a May 2006 date. As a point of comparison, Staff witness Schlaf pointed out that the first two New Jersey auctions were held nearly six months prior to the delivery dates for those auctions. (ICC Staff Exhibit 5.0, p. 19, lines 402-416) Dr. Schlaf's direct testimony showed that only later, as more auction experience was gained, did the gap between auction date and delivery date narrow to less than four months. (ICC Staff Exhibit 5.0, p. 20, Table 2) Dr. Schlaf also noted that ComEd proposed September 2006 as the date for the initial auction. (ICC Staff Exhibit 5.0, pp. 18-19, lines 398-399)

In rebuttal testimony, Ameren witness Nelson stated that the Ameren Companies and ComEd agreed on the first ten days of September 2006 as the timeframe for the initial auction. Mr. Nelson stated that the Ameren Companies believe that "the benefit of a single statewide auction date outweighs the benefits/detriments of either a May or September auction date." (Resp. Ex. 10.0 Corrected, pp. 14-15, lines 326-332) Mr. Nelson stated that the September 2006 date represented a reasonable balancing of interests. (*Id.*, lines 335-337)

CCG witness Smith was the only prospective bidder to respond to the September 2006 proposal. Mr. Smith, while still preferring the May 2006 date, stated that CCG would not object to simultaneous September auctions and that the September date would not affect CCG's desire to participate in the auctions. (CCG Exhibit. 2.0, p. 2, lines 38-43)

Staff supports a September 2006 date for the initial auctions. (ICC Staff Exhibit 13.0, p. 10, line 227) This date should resolve any concern that the Auction Manager will not have a sufficient amount of time following the Commission's order in this proceeding to complete the tasks that must be completed prior to the auction. These tasks include the testing of and practice with and software and supplier training. (ICC Staff Exhibit 13.0, p. 10, lines 227-232) It would be preferable to spend more time ironing out any problems upfront rather than, as CES suggests, scheduling the auctions at an early date and leaving September 2006 as a fallback date.

Thus, Staff recommends that the Commission approve the September 2006 auction date. Staff recognizes that holding the auctions in September 2006 would leave relatively little time prior to January 2007 should the Commission reject the auction results. Thus, Staff expects the Ameren Companies to have a contingency plan ready to present to Staff and the Commission in the event that the auction results are rejected. (ICC Staff Exhibit 13.0, p. 10, lines 232-235)

G. Common vs. parallel auction

The "simultaneous" in simultaneous descending clock auction has a technical meaning that we shall now make clear. As noted before, the SDCA is a simultaneous auction in that multiple products are auctioned at the same time. However, it is not merely that the products are bought separately but at the same time (i.e., in ***parallel***). Rather, the different products are bought within the same ***common*** auction. Furthermore, one of the important features of the SDCA is that bidders in the common auction are permitted to switch between products during the auction. That means that a bidder can go from offering 5 tranches of a product A and 3 tranches of a product B (in one round) to offering 4 tranches of each of the two products (in the next round).

There was some record debate over which products should be grouped together to be auctioned simultaneously, through a common SDCA auction, and which groups of products should be auctioned separately from other groups, in parallel. This sub-section reviews that debate. However, in Staff's view, the controversies that existed at the beginning of the case--over the common vs. parallel issue--have been resolved.

In its original filings, the Ameren Companies proposed that the various "fixed price" products should be grouped together and auctioned simultaneously, while the "hourly" product should be purchased in its own separate auction (held in parallel with the fixed price products auction).[7] ComEd made the same proposal in Docket No. 05-0159. In addition, the Ameren Companies proposed that its various products should be auctioned separately from ComEd's products (in parallel auctions). ComEd made the same proposal. By the rebuttal stage of the case, both the Ameren Companies and ComEd modified their proposals to allow:

- A common auction for all of the fixed price products of both the Ameren Companies and ComEd;
- A common auction for the hourly products of both the Ameren Companies and ComEd; but
- The two common auctions referenced above would be conducted in parallel in relation to each other.

Sub-section 1, below, addresses the appropriateness of using (i) a common auction for all the fixed price products, and (ii) a common auction for all the hourly products (the first two bullet points). Sub-section 2 addressed the appropriateness of *not* combining the fixed price products with the hourly products within a single common auction. Sub-section 3 makes special reference to the factors involved in deciding to group Ameren and ComEd products within the same auctions. Finally, Sub-section 4 addresses IIEC witness Dauphinais' recommendation to condition approval of a common auction on the establishment of a "common deliverability test."

[7] Recall from the earlier description of the full-requirements products that the "fixed price" products are fixed in the sense that all payments to the supplier would be based on a single price to be determined through the auction. The "hourly" product actually includes a fixed capacity charge to be determined through the auction, but all other payments to winning bidders for the "hourly" product would be formula based or index based (and hence not fixed). Most significantly, an energy charge component of the payment to suppliers would be tied to the hourly spot price in the relevant RTO energy market.

1. Among fixed price products and hourly products

a. Common auction for fixed price products

As noted above, in its initial filing, the Ameren Companies proposed to group together all of its fixed price products in order to acquire them through a single common simultaneous auction. ComEd made a similar proposal. Staff witness Salant praised the approach of combining products within a single common auction. He discussed the general efficiency gains and consumer benefits to the common auction approach (allowing switching or "arbitrage" between products) as opposed to the separate but parallel auction approach. (ICC Staff Exhibit 1.0, pp. 29-50) In fact, as discussed in the next few sub-sections, he argued that more of the Ameren and ComEd products should be auctioned simultaneously, within the same common auction.

b. Common auction for hourly products

In its initial filing, the Ameren Companies had only ***one*** hourly product. So did ComEd. In addition, both the Ameren Companies and ComEd, at that point, were not proposing to combine Ameren and ComEd products. Hence, for the Ameren Companies, a common auction for ***the*** "hourly" product would have been a nonsensical concept. The same was true for ComEd.

However, as discussed in sub-section 3, the issue of combining Ameren and ComEd products was raised by Staff witness Salant, and, along with it, the issues of combining all of the Ameren and ComEd "fixed price" products and all of the Ameren and ComEd "hourly" products. In rebuttal testimony, the Ameren Companies (in this docket) and ComEd (in Docket No. 05-0159) agreed to combine their "fixed price" product common auctions into a single common auction. They also agreed to combine the Ameren and ComEd "hourly" products into a single common auction for those two products.

With respect to the issue of ***at least*** combining all the "fixed price" products into a common auction and all of the "hourly" products into a common auction, there was no controversy after the rebuttal stage.

2. Between fixed price and hourly products

As noted above, in their rebuttal testimony, the Ameren Companies and ComEd agreed to hold two common auctions: (1) for all of their fixed-price products and (2) for both of their hourly products. They rejected Staff witness Salant's proposal to combine the fixed price and hourly products under just one common auction. In making that proposal, Dr. Salant noted that:

> [A]ccording to Dr. LaCasse, a utility's hourly price product is not a substitute for its fixed price products because the risks as well as the revenue streams facing the suppliers of the fixed price products and the hourly price products are different. …
>
> However, I note that the utilities do not cite any sources to justify their claim that suppliers do not perceive the fixed price and hourly price products to be substitutes. In addition, as discussed below, allowing suppliers to switch between the fixed price and hourly price products should impose little to no incremental costs on the utilities. I also reiterate the fact, as discussed above, that even a small number of suppliers engaging in arbitrage can have a significant effect on the auction prices.

(ICC Staff Exhibit 1.0, p. 43, lines 960-963 and lines 965-971)

However, in his rebuttal testimony, Ameren witness Nelson stated that "switching between the fundamentally different fixed-price and hourly-price products, whether between such products in an Ameren auction or between the ComEd and Ameren auctions is both unwise and risky, at least until further experience is gained with auction processes in Illinois." (Resp. Exhibit 10.0 Corrected, p. 3) In addition, Ameren witness LaCasse provided additional support for separately auctioning the “fixed price” and “hourly” products (Resp. Ex. 12.0, pp. 67-69), prompting this reply from Dr. Salant:

> [S]ince the capacity component of the fixed price contracts is, in Dr. LaCasse’s estimate, roughly 10 percent of the costs of the fixed price contract (Resp. Ex. 12.0, p. 68, lines 1614-1617), the potential benefits of combining the fixed-priced and hourly price contracts into a single auction are relatively small. For this reason, I recommend approval of Ameren’s proposal to combine auctions with ComEd, even though the fixed-price and hourly price products are to be auctioned separately.

(ICC Staff Exhibit 11.0 Corrected, pp. 11-12, lines 247-254)[8]

Based on the eventual concurrence between the witnesses who testified to the issue, and on the fact that no other party opposed the auctioning of the “fixed price” and “hourly” products separately (in parallel auctions), Staff recommends that the Commission approve the combining all of the Ameren and ComEd “fixed price” products in one common auction and all of the Ameren and ComEd “hourly” products in one common auction..

3. Between Ameren and ComEd products

As discussed above, ComEd and Ameren originally proposed to conduct their respective auctions separately (albeit in parallel). However, Staff witness Salant testified that

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[8] Dr. Salant also recommended that for future auctions, Ameren should “explore ways of separating the capacity and ancillary services from the energy component of the fixed price products in order to conduct a single auction for the capacity and ancillary services portion of those customer segments and the hourly priced customer segments.” This is clearly an issue for a later proceeding.

> Based on my discussions with suppliers, I understand that some suppliers have the resources to serve both Ameren and ComEd. In addition, in my discussions with suppliers, many suppliers indicated that their deployment of resources to serve Ameren's and ComEd's load would be based on the price differences between the products. That is, there appears to be both a need and an ability to switch between the products across utilities, and these exist despite the existence of any "seams" between the RTOs.

(ICC Staff Exhibit 1.0, p. 41, lines 911-918)

Furthermore, Staff witness Ogur's testimony

> (1) demonstrates that the claim of the Applicants' witness that the current stage of development of the MISO and PJM Interconnection ("PJM") joint and common market cannot support switching between ComEd and Ameren products in the auction is unconvincing, and (2) describes how bidders can work around these seams to effectively switch between the products of the two utilities.

(ICC Staff Exhibit 4.0, pp. 5-6, lines 95-100)

Mr. Ogur also reviewed the direct testimony of Ameren witnesses LaCasse. He observed that Dr. LaCasse provided no proof of her claim that "Ameren and ComEd products would be viewed as having dissimilar risks and characteristics by the suppliers if the joint and common market is insufficiently developed." (ICC Staff Exhibit 4.0, pp. 7-8, lines 151-155) She also failed to identify "any costs or drawbacks to allowing switching between Ameren and ComEd products in the current stage of development of the joint and common market." (*Id*., p. 8, lines 165-168)

In rebuttal, both the Ameren Companies and ComEd agreed to a common auction for both the Ameren and ComEd fixed-price products. Similarly, they agreed to a common auction for both the Ameren and ComEd hourly products. (see, for example: Resp. Ex. 10.0 Corrected, pp. 2-3)

Thus, Staff respectfully recommends that the Commission approve the proposal to combine Ameren products with the ComEd products, to the extent described above, in order to conduct two common auctions in parallel with each other: (1) a fixed price product auction consisting of several fixed price products; and (2) an hourly product auction consisting of two hourly products.

4. Common deliverability test

IIEC witness Dauphinais indicated that "a joint and common market for PJM and MISO is desirable, but not necessary to enable a joint auction." However, he also indicated that

> The disparate treatment of capacity resources should be removed in Illinois. This could be achieved by developing a ***common deliverability test*** for capacity resources within the combined MISO and PJM footprint to the combined ComEd and Ameren load zones in Illinois. I am not an attorney and cannot determine if the Commission can require MISO and PJM to establish such a joint deliverability test for Illinois only, or require Ameren and ComEd to do so on their own. However, the Commission can require Ameren to work with ComEd, MISO and PJM to establish a common deliverability test for Illinois load and a joint power procurement auction. In addition, the Commission can condition the continued use of procurement auctions on establishment of a common deliverability test and a joint auction by a date certain. Until a joint auction is implemented, the Ameren and ComEd auctions should be conducted in parallel, as discussed in the testimony of Mr. Collins.

(IIEC Exhibit 2 Corrected, p. 8, lines 168-179)

In his rebuttal testimony, Mr. Dauphinais restated his position on the common deliverability test:

> IIEC appreciates Ameren and ComEd's modified proposal to allow the switching of certain bidder offers between the Ameren and ComEd auctions. However, as I noted in my direct testimony, there will likely be very little switching of bidder offers between Ameren and ComEd (even under the modified proposal) because the capacity, or financial equivalent of capacity, underlying the bids would not be interchangeable between the Ameren and ComEd load zones (Direct Testimony of Dauphinais, IIEC Exhibit 2, at 6-8). Therefore, the proposed modification is of limited value unless the interchangeability issue is resolved. To resolve this issue, I

> proposed in my direct testimony that the Commission require Ameren to work with ComEd, Midwest Independent Transmission System Operator, Inc. (MISO) and PJM Interconnection, LLC (PJM) to establish a common deliverability test for capacity resources within the combined MISO and PJM footprint to the combined Ameren and ComEd load zones in Illinois (Id. at 8-9). The continued lack of such a test will frustrate the promised improvement in the auction process.

(IIEC Exhibit 5, p. 3, lines 33-46)

In cross-examination, Mr. Dauphinais clarified by stating,

> I believe some type of initial auction could go forward without an accountability test. But at some point in the future at a date certain it should be there.

(Common Tr., p. 126)

Having reviewed his testimony, Staff is not certain ***exactly*** what Mr. Dauphinais is recommending. Clearly, he wants the Commission to "Ameren to work with ComEd, Midwest Independent Transmission System Operator, Inc. (MISO) and PJM Interconnection, LLC (PJM) to establish a common deliverability test for capacity resources within the combined MISO and PJM footprint to the combined Ameren and ComEd load zones in Illinois." With respect to this recommendation, Staff takes no position. Furthermore, it does ***not*** appear he is recommending that approval of the Ameren Companies' and ComEd proposed auctions be withheld until such a test is established. With respect to this position, Staff is in agreement with Mr. Dauphinais.

However, Mr. Dauphinais ***may*** also be recommending that approval of a common auction for both Ameren and ComEd products be withheld until such a common deliverability test is established, but the wording of his testimony leaves considerable ambiguity. For example, recall from his direct testimony, Mr. Dauphinais indicated that

> [T]he Commission can condition the continued use of procurement auctions on establishment of a common deliverability test and a joint auction by a date certain. Until a joint auction is implemented, the Ameren and ComEd auctions should be conducted in parallel, as discussed in the testimony of Mr. Collins.

(IIEC Exhibit 2 Corrected, p. 8, lines 176-179)

Notwithstanding the ambiguity, if his recommendation is that approval of a common auction for both Ameren and ComEd products be withheld until a common deliverability test is established, then Mr. Dauphinais' recommendation should be rejected. The testimony of numerous witnesses indicates that there are benefits to a common auction, even if the seams between MISO and PJM are not completely eliminated. (See excerpts from the testimony of witnesses Salant and Ogur in the sub-sections 1 through 3, above)

H. Blended, Fixed Price Auction Products

1. Proposed blends for residential and small commercial customer supply

a. 3-year agreements

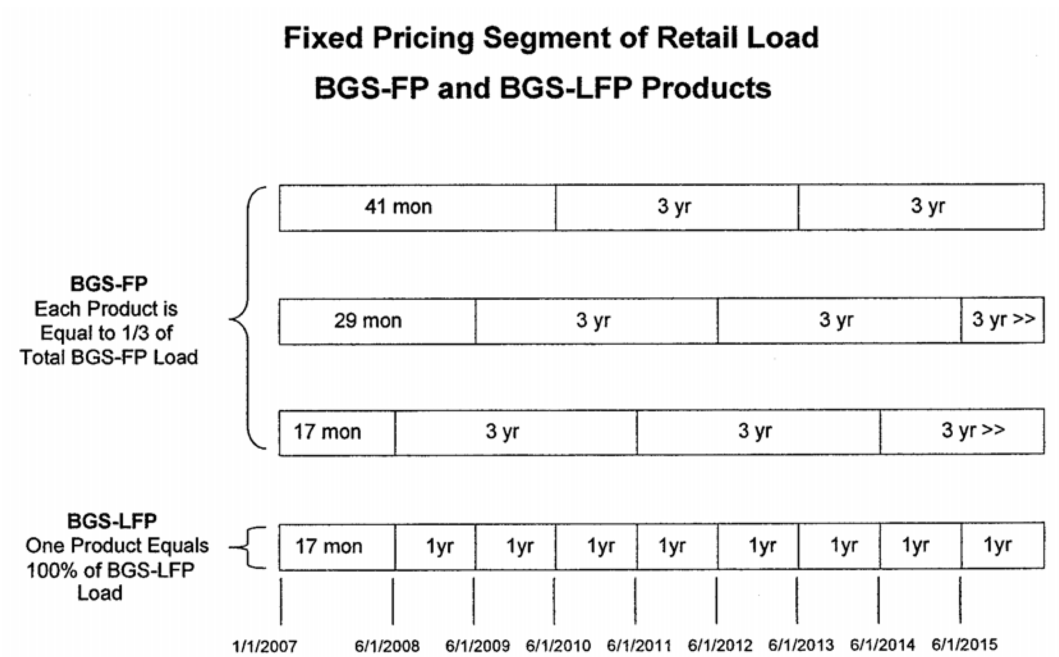
For the majority of its customers (i.e., those with peak demands under 1 MW, which Ameren calls the "BGS-FP" segment), the Ameren Companies propose to maintain an annually-revised portfolio of 3-year supply contracts. Delivery under each contract would begin in June and end 36 months later in May. However, in the initial auction, delivery must begin in January, due to the December 31, 2006 expiration of the Ameren Companies' existing supply contracts. Hence, in the initial auction, each of the 3-year contracts would include an ***additional*** 5 months (January through May of 2007). Furthermore, in order to effectively transition to an annually-revised portfolio of 3-year supply contracts, it is also necessary to include within the initial auction some 2-year, and 1-year contracts (all of which would also include the extra 5 months for January through May of 2007).

In Staff's opinion, this proposal is greatly facilitated by a schematic diagram, such as the one below, which shows the phase-in of both the BGS-FP contracts (for customers with peak demand under 1 MW), as well as the BGS-LFP contracts (for customers with peak demand over 1 MW.

Ameren witness Blessing attempted to justify this annually-revised portfolio of 3-year supply contracts, stating

> In order to provide market-based yet reasonably stable pricing for this group of small customers, the Companies intend to procure overlapping three-year contracts in which one-third of the R&SB load is procured every year. While there may be variations in the market from year-to-year, overlapping three-year contracts will serve to stabilize or smooth out price fluctuation.

(Resp. Ex. 3.0, p. 6, lines 118-122)



Source: Resp. Exhibit 4.1

The appropriateness of the proposed overlapping 3-year durations for BGS-FP contracts was an issue in the case. AG witness Salgo recommended that Ameren perform an analysis of contract durations, arguing that

> [I]n principle, I am not opposed to longer term contracts. In this situation, however, the Company has not presented a rationale for 'testing' the market for three year, full requirements, fixed price contracts. These are high priced, premium products that shift all management of volume and fuel price risk to each supplier, while relieving the purchaser (*i.e.,* the utility) from all management responsibility. Does the Company believe that the bundled-service customers would be better off with these 3-year, full requirements contracts than if it were to shorten the contract durations more generally or use alternative contract terms? Given the size of the proposed procurement, the answers to these questions have enormous financial implications and need to be addressed in this proceeding."

(AG Exhibit 2.0, p. 14, line 15-p. 15, line 2)

DES/USESC witness Steffes recommended three-month contract durations for customers that use 15,000 kWh per year or less. (DES/USESC Ex. 1.0, pp. 8-9) Ameren witness Blessing responded to Mr. Steffes' proposal, opining that

> Mr. Steffes is not proposing simple modifications to the product design, rather he is proposing radical changes based on a fundamental difference of opinion as to customer's desire to have reasonably stable rates and the utilities' role in providing those reasonably stable rates.

(Resp. Ex. 11.0 (Revised), p. 30-31, lines 681-684) Staff witness Zuraski also argued against Mr. Steffes' proposal, and noted that 15,000 kWh is not much more than the average annual use per residential customer. (ICC Staff Exhibit 12.0, p. 9, fn. 5)

With respect to Mr. Salgo's recommendation that Ameren perform an analysis of contract durations, Staff witness Zuraski opined,

> [I]t is not clear what Mr. Salgo wants the Company to do that the AG could not do itself, with the aid of Mr. Salgo or other experts. I share his desire for a thoughtful consideration of the options for defining the products to be acquired through the auction. However, I do not understand why it cannot be done in the context of the current docket.

(ICC Staff Exhibit 12.0, p. 9, lines 198-202)

In addition, Staff witness Zuraski presented a risk assessment analysis (*Id.*, pp. 10-20), with which he demonstrated:

> First, the price of the longer-term contracts may entail an excessive risk premium.

(*Id.*, p. 10, lines 205-206) He also argued:

> Second, if there is a significant expected upward or downward trend market prices, the longer-term contracts will induce uneconomic retail switching activity. Third, as with any new process, the possibility of discovering problems or errors is higher for the initial implementation of the auction and will diminish over the course of subsequent auctions as problems are discovered and remedied on a going-forward basis. However, the length of time that is required before any remedial measures can take effect generally will be tied to the length of the supply contracts. In this regard, it may make more sense to test the waters with shorter-term contracts until all the problems with the auction (if any) have been identified and, if possible, eliminated or ameliorated.

(*Id.*, lines 206-215)

Mr. Zuraski concluded:

> First, while I am concerned about the potential risk premiums associated with using long-term contracts, I have not provided what I would consider to be reliable predictions of those premiums. Second, in the 2004 NJ auction, both 1- year and 3-year contracts were auctioned simultaneously, and the actual differences in prices between the 1-year and the 3-year products were less than one percent for three of the utilities and 2.87% for the remaining utility. Third, in the first auction, only 33% of demand will be served from 3-year contracts, allowing a comparison with 2-year and 1-year contract prices. Fourth, to the extent to which ratepayers and the Commission may be adverse to price volatility, including long-term contracts in the blend should reduce exposure to such volatility.
>
> Finally, it is worth remembering that the use of 3-year durations is not being written in stone. There will be opportunities to periodically review the auction results and reassess the mix of contracts to be procured in future years. Thus, for the time being, Staff recommends that the Commission accept the Company's proposed use of 3-year contracts, and that the Commission reassess the benefits and costs of using this contract duration at points in the future.

(*Id.*, pp. 21-22, lines 435-451)

In summary, the weight of the evidence supports adoption of Ameren's proposal for an annually-revised portfolio of 3-year supply contracts for serving the residential and small commercial customer included in the so-called BGS-FP segment. In Staff's view, at this time, there is no evidence of a better way of obtaining "market-based yet reasonably stable pricing," as articulated by Ameren witness Blessing. (Resp. Ex. 3.0, p. 6) Staff would be particularly concerned with proposals to use contracts of less than 1 year, considering such alternatives inconsistent with obtaining price stability. Staff would also be opposed to making significant greater use of long-term contracts, such as 5-year or longer. Such alternatives would be inconsistent with obtaining market-sensitive pricing and could entail significant risk premiums for the reasons fully explained in Mr. Zuraski's testimony. (ICC Staff Exhibit 12.0, pp. 8-22)

Thus, for all the above reasons, Staff respectfully recommends that the Commission approve the Ameren Companies' proposal for an annually-revised portfolio of 3-year supply contracts for serving the residential and small commercial customer included in the so-called BGS-FP segment, along with the transitional use of other contract durations during the initial auction in order to arrive at this eventual steady state.

b. Percentage of supply acquired at subsequent auctions

With respect to percentage of supply acquired at subsequent auctions, see Staff discussion in sub-section a above. Staff reserves the right to respond in its reply brief to parties that address this matter in their initial briefs.

2. Proposed 1-year fixed price product for 400kW-1MW customers

According to CES witness O'Connor,

> The Coalition recommends that the BGS-FP customer grouping should be bifurcated at the 400 kW level. Larger business customers within the 400 kW to 1 MW demand group would be separated from all those below that level and offered a one-year, fixed price product akin to that offered to customers over 1 MW in demand, that we can call "BGS-LFP2." However, that product would be an automatic default product for customers with less than 1 MW in demand, not requiring an affirmative election.
>
> Under this approach, the small customer grouping, residential and smaller commercial retail customers with peak demands up to 400 kW, would continue to be offered the one-year, fixed-price product based on the blended multi-year, laddered auction product.

(CES Exhibit 1.0, pp. 13-14, lines 289-300)

In reaction to this proposal, Staff witness Zuraski opined

> In principle, Staff supports this proposal. As explained in the previous section of my rebuttal testimony, I am concerned that long-term supply contracts, combined with giving customers relative freedom to switch between RES supply and auction-derived Company supply, will lead to significant risk premiums being built into auction prices. It is reasonable to believe that switching in order to take advantage of price changes will be most pronounced for the largest customers in the BGS-FP customer segment (i.e., those within the 400 kW to 1 MW sub-group). According to Ameren witness Blessing, "switching risk is greater for larger customers than for smaller customers." (Resp. Ex. 11.0 (Revised), p. 26, lines 571-572)
>
> Removing the 400 kW to 1 MW customers from the BGS-FP segment--and placing them in their own segment to be served with one-year contracts--would allow the market to decide directly what the switching risk premium for the 400 kW to 1 MW sub-group should be, thus bypassing the issue of whether to perform a computational allocation of the risk premium facing the entire BGS-FP segment. In addition, since the 400 kW to 1 MW sub-group seems to comprise the customers with the highest propensity to switch to delivery services, segregating them from the BGS-FP segment can be expected to reduce the switching risk premium embedded in the auction prices of the revised BGS-FP segment, thus lowering the rate for the smaller customers. In fact, the total amount

> of switching-risk premiums paid to suppliers should also decrease since the new 400 kW to 1 MW segment would be served with only 1-year contracts rather than the longer-term contracts that I have argued lead to higher risk premiums.

(ICC Staff Exhibit 12.0, pp. 23-24, lines 469-492)

However, Ameren witness Blessing argued that the Ameren Companies should not be too aggressive about tailoring retail power and energy services to various customer classes (Resp. Ex. 11.0 (Revised), pp. 21-23), opining,

> [T]he Ameren Companies should behave in a manner consistent with their role as wires companies and not as companies offering a variety of retail generation products to meet specific end use customer needs. … The Ameren Companies, as IDCs, should not be competing with ARES.

(*Id*., p. 22, lines 497-503)

Ameren witness Cooper raised a more practical concern, claiming that 90% of the customers in the 400 kW to 1 MW size range do not have the interval meters that would be necessary for them to be carved out of the BGS-FP segment. (Resp. Ex. 15.0, pp. 18-21)

Staff witness Zuraski rejected Mr. Blessings musings, testifying:

> While I agree that policy and rate structures should be designed to allow competitive forces to take hold in Illinois retail electric markets, utilities should not be purposefully pricing themselves out of the retail market (for example, by offering poorly-designed products). If there are valid reasons to expect that placing 400 kW to 1 MW customers in the BGS-FP segment (to be served with relatively long-term-contracts) will raise rates for all customers in that segment, such product design can be inconsistent with the Company's obligation to provide least-cost service.

(ICC Staff Exhibit 12.0, p. 24, lines 506-514)

However, with respect to Mr. Cooper's argument, he stated,

> I would agree with Mr. Cooper that CES witness O'Connor's proposal to segregate the 400 kW to 1 MW customers presents a practical problem if these customers do not have interval metering. Hence, I recommend that Dr. O'Connor's proposal be placed in abeyance pending review of one or

more rounds of auction results and subsequent switching activity by customers within the BGS-FP segment. Meanwhile, I would request that the Company present estimates in its surrebuttal testimony of how quickly the Company could install interval meters on customers within the 400 kW to 1 MW size range, as well as the cost of such installation.

(*Id.*, p. 25, lines 516-524)

In surrebuttal, Mr. Cooper supported Mr. Zuraski's position, and, in reply to the data request, Mr. Cooper testified that

> The Ameren Companies estimate approximately 1,100 meters would need to be installed and these installations could be completed within two years of the start of replacements at a cost of approximately $280,000. In addition, the Ameren Companies would incur approximately $85 per meter per year ($95,000 annually) in ongoing processing expenses associated with data management of interval meter data.

(Resp. Ex. 22.0, pp. 19-20, lines 437-442)

Staff notes that for customers of at least 400 kw, these costs are trivial.[9]

Based on the above analysis of the issue, Staff respectfully recommends that Dr. O'Connor's proposal be placed in abeyance pending review of at least one round of auction results and subsequent switching activity by customers within the BGS-FP

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[9] This can be shown over a wide set of assumptions, as below:

Total cost of new meters		$280,000	Plus annual maint. cost per meter	Total cost per meter (1st year only)
Number of new meters		1,100		
Cost per meter		$254.55	$85.00	$339.55
Peak Load	Load Factor	Annual kwh	**Cost per meter (cents per kwh):**	
			After 1st yr	**1st yr only**
400 kw	30%	1,051,200	**0.0081**	**0.0323**
	40%	1,401,600	**0.0061**	**0.0242**
	50%	1,752,000	**0.0049**	**0.0194**
	60%	2,102,400	**0.0040**	**0.0162**
	70%	2,452,800	**0.0035**	**0.0138**
	80%	2,803,200	**0.0030**	**0.0121**

segment. Nevertheless, given the relatively low cost of installing the interval meters that would be necessary for the 400 kw to 1MW customers to be carved out of the BGS-FP segment, Staff does recommend that the Commission direct the Ameren Companies to begin the process of ensuring that all such customers will have the such meters installed within approximately two years.

3. Proposed Monthly and Quarterly products

As described in sub-section 1, above, the Ameren Companies proposed that retail customers with demands up to 1 MW be offered an annually-revised retail product, which the Companies would provide through an annual auction for 3-year fixed price wholesale supply contracts. However, DES-USESC witness Steffes recommended that:

(a) customers with annual peak demand under 1 MW and annual usage greater than 15,000 kWh (and that have not been declared competitive), should only be eligible for a monthly-revised retail product, which the Company would provide through monthly auctions for 1 month wholesale supply contracts; and

(b) customers with annual usage less than or equal to 15,000 kWh (and that have not been declared competitive), should only be eligible for a quarterly-revised retail product, which the Company would provide through quarterly auctions for 3 month wholesale supply contracts. (DES-USESC Ex. 1.0, pp. 29-31; and Common Tr., pp. 523-524)

Ameren witness Blessing disagreed with this recommendation, calling Mr. Steffes' proposal a "radical" change, which would not facilitate stable rates and mitigate volatility. (Resp. Ex. 11.0 (Revised), p. 31) Mr. Blessing also criticized Mr. Steffes' analogy to the monthly purchased gas adjustment clauses commonly used by Illinois gas utilities:

> While Mr. Steffes may be correct that the purchased gas adjustment (PGA) portion of a customer rates may indeed change monthly, this does not necessarily mean that these monthly PGA prices are composed of transactions with one-month terms entered into the month prior to delivery. In fact, it is my understanding that the contracts underlying this "monthly price" may be of much greater duration than one month. The natural gas industry relies upon many instruments including long-term hedge contracts to mitigate the volatility of the daily and monthly markets.

(*Id*., pp. 33-34, lines 728-735)

To support his latter point, Mr. Blessing noted a couple of examples. With respect to the Ameren Companies, for instance, "it is standard to use contracts of up to 6 years and in general less that 25 % of the total winter gas supply is priced at daily market rates." (*Id*., p. 35) In contrast, under Mr. Steffes' proposal, 100% of the load would be up for auction each month.

Mr. Blessing also criticized Mr. Steffes' proposal from the standpoint of practicality and cost-effectiveness, noting that

> Under Mr. Steffes proposal, the Ameren Companies would be required to run an auction each and every month in order to procure fixed price service for its R&SB customers with annual usage greater than 15,000 kWh. They would also be required to hold auctions on a quarterly basis for their R&SB customers with annual usage less that 15,000 kWh. What Mr. Steffes does not seem to consider when making this proposal is the time and expense required to set up and run a descending clock auction and the time and expense required on the part of suppliers to participate in this type of auction. Not only would it be extremely expensive and inefficient to hold monthly auctions, it simply is not practical. The time that is required to set up, promote, complete the application process and actually run an auction is approximately 5 months. …
>
> In addition, under Mr. Steffes' proposal, the expense of setting up and running a single auction along with the expense of suppliers to

> participate in a single auction will be spread over a very small number of MWh that these customers use over the course of a single month.

(*Id.*, pp. 34-35, lines 771-788)

Finally, Mr. Blessing argued that Mr. Steffes' proposal could lead to a less competitive auction, higher auction prices, and fewer tranches being filled:

> [P]articipation in an auction such as been proposed by the Ameren Companies requires an investment of time and money on the part of suppliers. It is very possible that suppliers will not be willing to make such an investment if winning earns them only a one-month contract. If suppliers choose to not participate this could result in a less competitive auction and higher auction prices could result. Another negative effect could be insufficient participation to procure 100% of the load in the auction. This would result in unfilled tranches being filled in the MISO spot markets and even more price volatility of the R&SB customers.

(*Id.*, pp. 35-36, lines 795-803)

Like Mr. Blessing, Staff witness Zuraski also disagreed with Mr. Steffes' "more extreme recommendation of using only contracts of one month duration for customers above 15,000 kWh and three months duration for all customers with annual usage below 15,000 kWh." (ICC Staff Ex. 12.0, p. 9, lines 193-196, footnote omitted) In a footnote, Mr. Zuraski also pointed out that "Between 2003 and 2004, the average annual use per residential customer for the four Ameren electric distribution companies in Illinois ranged between 10,000 and 11,500 kWh." (*Id.*, p. 9, fn. 5) Furthermore, Staff witness Salant noted that "Ameren will attract more bidders, and more offers per tranche, with one large auction than it would with a sequence of smaller auctions because a larger auction is likely to attract more bidder interest. Increased bidder participation should result in a more competitive auction." (ICC Staff Exhibit 11.0 Corrected, p. 70, lines 1605-1609)

Notwithstanding Mr. Blessing's critique, in his rebuttal testimony, Mr. Steffes argued that his proposal would help promote "a vibrant retail market," and that Ameren's proposal fails to take advantage of "a critical opportunity to foster a marketplace where numerous retail electric suppliers compete to serve customers, enhancing overall customer service and allowing new innovative products to come into the market." (DES/ESESC Ex. 2.0, p. 12, lines 249-252)

Staff disagrees completely with Mr. Steffes' assessment. The Companies' auction proposal places absolutely no restrictions on the ability of customers to switch to alternative retail suppliers. It does absolutely nothing to prevent entry of alternative suppliers; nor does it hinder them from offering and providing whatever services they wish to offer. Alternative retail suppliers would neither be impeded from "enhancing overall customer service" nor from inventing "new innovative products." From Staff's perspective, Mr. Steffes' proposal would try to give alternative suppliers an artificial advantage over Ameren's BGS-FP service, simply by degrading the BGS-FP service to a form that is less desirable to customers. As Staff witness Zuraski noted, in a similar context,

> While I agree that policy and rate structures should be designed to allow competitive forces to take hold in Illinois retail electric markets, utilities should not be purposefully pricing themselves out of the retail market (for example, by offering poorly-designed products).

(ICC Staff Exhibit 12.0, p. 24, lines 507-510)

Based on review of the record and for all the reasons given above, Staff respectfully recommends that the Commission reject DES-USESC witness Steffes' proposal that (a) retail customers with annual peak demand under 1 MW and annual consumption over 15,000 kWh should only have access to a monthly-updated Ameren energy product based on one-month wholesale contracts secured through auctions; and (b) retail customers with annual consumption up to 15,000 kWh should only have access to a quarterly-updated Ameren energy product based on three-month wholesale contracts secured through auctions.

I. Fixed price auction product and tariffed services for larger customers

1. Nature of auction product and tariffed services for 1 MW and over customers

The Ameren Companies proposed to provide a full-requirements annual, single fixed-price product (i.e., prices would be set for the length of the supply period) for customers with a peak demand greater than 1 MW ("BGS-L" service customers). BGS-L customers must remain on that service for the entire supply period (17 months for the first auction and 12 months for all subsequent auctions). The Ameren Companies believe that procuring the BGS-L product separately from the product offered to smaller customers will better align any switching risk premium that bidders may incorporate into their bids with the customer group creating such risk, and the requirement that BGS-L customers remain on that service until the next supply period will help reduce any switching risk premium. (Resp. Ex. 3.0, p. 4, lines 79-90)

2. Prequalification of BGS-LFP load

In order to allow potential suppliers to more accurately determine the potential load of large customers, IIEC witness Stephens recommended that customers be asked to "pre-qualify" their loads for the auction. Under this plan, customers would indicate whether they had any contractual commitments preventing them from taking the Ameren generation service. Mr. Stephens noted that a customer prequalifying its load would not be making a commitment to accept the auction price; rather, the prequalification would serve as an "affirmative indication of eligibility." (IIEC Exhibit 1, p. 13, lines 267-269) Staff has no opposition to this proposal, as it may tend to reduce any risk premium that wholesale suppliers might consider adding to their bids. For this reason, Staff recommends that the IIEC's prequalification proposal be adopted by the Commission.

3. Demand charge component for ≥ 1MW customers

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

4. Other

Staff reserves the right to respond in its reply brief to parties who raise other issues regarding fixed price auction product and tariffed services for larger customers in their initial briefs.

J. Contingencies

The Ameren Companies' proposed contingency plans that would be invoked should the Company need to purchase power outside of an annual auction. The contingency plans can be grouped into three categories: (1) undersubscription of the auction; (2) supplier default; and (3) Commission rejection of the auction results. (ICC

Staff Exhibit 5.0, p. 14, lines 301-306) In each of these scenarios, the Companies would have few supply options available should power be needed. (*Id.*, p. 16, line 336) That is, the Ameren Companies' potential supply options would be limited to: 1) spot market purchases from the MISO energy market, 2) bilateral negotiations with potential suppliers of capacity, or 3) holding a competitive acquisition solicitation process.

The three contingency scenarios as well as the Companies' proposed supply plans for each of the scenarios are discussed below. In most of the situations in which the Ameren Companies would require the implementation of a contingency plan, the Companies propose to purchase power directly through the MISO spot market. Staff finds the Companies' proposed reliance on the MISO spot market as their primary supply source under certain contingency scenarios to be appropriate. From an administrative standpoint, spot market purchases would be the most convenient means to purchase electricity, and perhaps also the least costly. Another advantage of using the MISO spot market is that, to the extent that the MISO spot market is competitive, any concern that a large seller might influence the market price would be minimized. (ICC Staff Exhibit 5.0, p. 17, lines 358-364) Similarly, Ameren's choice of a replacement competitive acquisition solicitation process for certain scenarios meeting specified conditions also appears reasonable and appropriate based on a consideration of applicable benefits and costs.

As explained in more detail below, Staff has no objection to the procurement methods outlined in the contingency plans as proposed by the Ameren Companies.

1. Volume reduction

The first contingency scenario, undersubscription of the auction, addresses the fact that the auction rules allow for a reduction of the tranches to be procured through an auction in certain circumstances. For instance, the Auction Manager may reduce the volume of tranches to be procured in an auction if there is insufficient interest in the auction to ensure competitive auction prices. (Resp. Ex. 3.0, p. 19, lines 409-410) In the event of a volume reduction the Ameren Companies propose to procure the unfilled tranches of BGS supply through the MISO spot market. (Resp. Ex. 3.0, p. 19, lines 415-421; Resp. Ex. 12.0, p. 43, lines 1040-1042) Ameren witness Blessing testified that bidders would have a diminished incentive to participate in the auction if they believe that an undersubscribed auction would allow bidders to negotiate supply contracts outside the auction. (Resp. Ex. 3.0, pp. 19-20, lines 422-433)

Staff agrees with the Companies' that, in a volume cutback scenario, purchasing power from the MISO spot market would be preferable to the alternatives of conducting bilateral negotiations with other suppliers or holding another auction. As Ameren witness Blessing explained, if bidders thought that an undersubscription would cause the Companies to enter into direct negotiations with suppliers for the undersubscribed supply they would have a reduced incentive to bid in the auction or, if they participated in the auction, might alter their bidding strategies. Holding a second auction to replace the power that was not purchased in the original auction might seem to be a viable strategy, but, given that the first auction is undersubscribed in this scenario, it is uncertain that a second auction would attract more supplier interest than the initial auction. (ICC Staff Exhibit 5.0, p. 16, lines 336-346) As a result, Staff agrees that a second auction does not appear to present a viable contingency option.

Staff believes, however, that one clarification needs to be made with respect to application of this contingency scenario. In the event that the Commission rejects the results of an auction, all of the tranches originally to be procured through the rejected auction – including any tranches not auctioned due to volume reductions – should be handled pursuant to the "rejection" contingency provisions rather than the "undersubscription" contingency provisions. If this were not the case, the portion of the Companies' load requirements that were separated from the auction due to the volume reductions would be purchased using the supply options prescribed in the "undersubscription" contingency plans, while the rest would be purchased according to the "rejection" contingency provisions. It would thus be possible that the supply option used to purchase the power that was not auctioned would be different than the supply option or options that the Commission approves under the rejection contingency provisions. A determination by the Commission to reject the results of an auction indicates some problem or issue beyond the circumstances giving rise to a volume reduction. In this situation, the appropriate replacement supply plan for the entire auction load should be determined in view of whatever facts gave rise to the rejection – which is what occurs through application of the "rejection" contingency scenario.

Thus, Staff does not object to the contingency plan for volume cutbacks provided that in the event that the Commission rejects the results of an auction, all of the tranches originally to be procured through the rejected auction – including any tranches not auctioned due to volume reductions – are to be subject to the "rejection" contingency provisions.

2. Supplier default

If a supplier defaults during the supply period, and more than 90 days remain until the next auction, the Ameren Companies propose to purchase replacement power under a Request for Proposal ("RFP") process. The product sought in the RFP would be the same as the product purchased in the auction. The Ameren Companies would procure power through the MISO spot market until the successful RFP bidders start to deliver power. (Resp. Ex. 3.0, p. 20, lines 449-459) Staff has no objection to these plans, as replacement power would be purchased through competitive acquisition processes rather than through direct negotiation with wholesale suppliers. If less than 90 days remain until the next auction, the Companies' contingency plans calls for replacement purchases from the MISO spot market. (Resp. Ex. 3.0, p. 20, lines 445-448) As noted above, there is adequate justification to purchase power through the MISO spot market pending completion of the competitive acquisition process. (ICC Staff Exhibit 5.0, p. 17, lines 356-364)

3. ICC rejection

As noted above, the "rejection" contingency scenario addresses the situation where the Commission rejects the results of an auction. The Ameren Companies' proposal to develop a supply plan, confer with Staff, and bring the supply plan to the Commission for approval in the event of a rejection is acceptable to Staff. (Resp. Ex. 3.0, pp. 21-22, lines 474-488; ICC Staff Exhibit 5.0, p. 16, lines 351-354) Auction failure (except for reasons that can be easily corrected by immediately re-running the auction) would mean that a new supply strategy is needed, and needed promptly, to ensure power delivery in 2007. However, in the event of an auction failure that cannot be remedied quickly, Staff expects that the Companies would be prepared to promptly propose a supply plan in the event of Commission rejection of the auction results. (ICC Staff Exhibit 13.0, p. 10, lines 232-235) As noted above, this contingency option should apply to all load (tranches) that were originally set for procurement through the rejected auction – including any tranches not auctioned due to volume reductions.

4. Subsequent prudence reviews of actions in response to contingencies

It is Staff's understanding that the Ameren Companies seek a prudence determination in this proceeding for all purchases to be made pursuant to the auction proposal, including purchases to be made pursuant to the alternative procurement methods for the contingency scenarios described above. (See Resp. Ex. 2.0., p. 24, lines 533-535, pp. 25-26, lines 541-546, 551-556; Resp. Ex. 6, p. 66) As will be discussed below, Staff agreed in part and disagreed in part with the Ameren Companies' request for a full, complete and across-the-board prudence determination for its proposed contingency purchases. As of the close of the hearings, the Ameren Companies and Staff were in agreement that the Companies' request for a prudence determination with respect to the contingency scenarios exempted or excluded certain aspects or types of issues under those scenarios. In general, the Ameren Companies clarified that – with respect to the contingency scenarios – it is not seeking a prudence determination where it will be taking future discretionary action, which may or may not be prudent under applicable legal standards, that could cause the need for such purchases or impact the net amount to be charged to ratepayers for such purchases.

With this understanding and limitation, as explained in more detail below, Staff supports the Companies' request for a prudence determination for the alternative procurement methods outlined in its contingency scenarios.

With respect to the potential contingency purchases at issue here, there are three general aspects to a prudence determination. The first area of inquiry is whether the proposed purchases themselves will result in prudently incurred reasonable costs. In other words, the first issue is whether the prices to be paid pursuant to the contingency procurement methods should be pre-approved as just and reasonable. Staff concurs with the Companies' request that the Commission find the contingency purchases to be made through the MISO or through an RFP process will result in prudently incurred reasonable costs for such supply. As discussed above, these contingency supply options represent reasonable supply sources that will not negatively impact the competitiveness of the annual auctions. The use of these supply options should produce the most convenient and least costly supply, taking into account the amount of load to be procured and the cost of running the replacement procurement process. (*See* ICC Staff Exhibit 5.0, p. 17)

Although Staff supports a prudence finding for the prices to be paid through these procurement methods, there is one limitation that should be made clear. As discussed above, the Ameren Companies' contingency plan in the event the Commission rejects the results of an auction is to develop a new supply plan to be brought to the Commission for approval. Obviously, it would be premature to pre-approve the prudence of supply plans that have not been developed, including the prices that would result from such unspecified plans.

A prudence inquiry for contingency purchases does not end with an examination of price considerations. The second area of prudence inquiry is an analysis of the reasons for the purchase.[10] It is well established in Illinois jurisprudence that "the prudency standard [is applied] not only to the actual purchase amounts but [also] to the reasons for those purchases . . . ." (United Cities Gas Company v. Illinois Commerce Comm'n, 163 Ill. 2d 1, 17-18 (1994)) In other words, if a utility's imprudent acts or omissions cause certain costs to be incurred (i.e., the reasons for the purchase), then those costs are not prudent notwithstanding the prudence of the price paid or quantity purchased since the utility would not have incurred those particular costs if its acts or omissions causing the need for the purchase had been prudent. As is obvious from the "contingency purchases" description, the present analysis focuses on how the Companies will procure power in the event that certain future events develop and prevent it from procuring power and energy through the SFCs resulting from annual auctions. Since those facts will occur in the future, a full prudence determination cannot be made here, and the Commission must retain the right to review the Companies' prudence in light of the facts that do develop.

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[10] Staff notes that this inquiry is a non-issue for the auction-based SFC purchases. Those purchases are the original purchases made to fulfill the Ameren Companies' statutory obligation to continue to provide bundled service to retail customers. 220 ILCS 5/16-103(a). Further, because the auction product is a full requirements product for which the supplier agrees to provide a fixed percentage of the Ameren Companies' load and assumes all volume risks, there appears to be no imprudent action that the Ameren Companies could take with respect to the reasons for or the volume of the supply purchased. In other words, the only real inquiry for the auction-based purchases is whether the prices that will result from that process will be just and reasonable. As discussed in other portions of this brief, the record in this proceeding fully supports a finding that the Ameren Companies' auction proposal as modified by Staff will result in prudently incurred reasonable costs (subject, of course, to the Commission's ability to reject the auction results).

The third area of prudence inquiry with respect to the potential contingency purchases at issue here is whether the Companies have acted prudently with respect to the credit requirements. The credit requirements serve several purposes including reasonable assurance of the credit worthiness of the suppliers and protection against losses in the event of a supplier default. In particular, certain credit instruments required under the SFCs are intended to provide an offset in the event that a supplier defaults and the then current cost of replacement power is higher than the contract price. Again, certain facts with respect to the Companies' management of its credit requirements and the impact of such acts or omissions on the amounts to be paid by retail customers will not be known until they occur in the future, and the Commission must maintain the ability to review those facts when they occur.

Thus, while Staff supports the Ameren Companies' proposed contingency plans, Staff believes that it is premature to provide an across the board finding that all purchases made pursuant to those plans will constitute prudently incurred reasonable costs because the future events and actions triggering the contingency provisions or impacting implementation of the credit requirements are relevant to a final determination of prudence and are not known at this time. These concerns with respect to prudence were discussed by Staff witness Schlaf and Staff witness Phipps. (ICC Staff Exhibit 5.0, pp. 17, lines 369-375 and ICC Staff Exhibit 15.0, pp. 4-5, lines 74-79) As discussed in Section VII.B.5 below, the Companies do not oppose tariff language proposed by Staff witness Schlaf that specifically maintains the Commission's ability to review the prudence of the contingency purchases with respect to future acts or omissions by the Ameren Companies that contribute to the need for such purchases or impact the net amount to be charged to ratepayers for such purchases. Under this language, the Commission could commence a proceeding to determine whether the contingency purchases were required because of an act or omission by the Companies, whether the net amount charged to ratepayers was impacted by an act or omission by the Companies, whether the act or omission was imprudent, and, if so, whether the amount charged was unreasonable. Staff submits that the record in this proceeding supports the Companies' request for a prudence determination with respect to supply charges for purchases under the contingency provisions subject to an express reservation of the Commission's ability to conduct a limited prudence review as described above.

K. Regulatory oversight and review

1. Nature of Commission review before, during, and after Auction

The Ameren Companies auction based competitive procurement proposal provides for regulatory oversight and review of the auction proposal, the auction process and the auction results. The most significant and fundamental review of the Ameren Companies' proposal is the instant proceeding where the Commission will determine whether it is appropriate to approve that proposal based on the evidence and arguments submitted by the parties. Indeed, it is in this proceeding where the traditional ratemaking decisions pursuant to the Illinois Public Utilities Act will be made, and the numerous issues presented by this filing are discussed in detail in other portions of this brief.

Staff notes here that certain Intervenors appear to have concerns regarding the Companies' request for approval of their rider proposal, including a request for a current determination that the rider based rates are just and reasonable. Staff submits that it is totally appropriate to make that fact-based determination in this proceedings. The Ameren Companies' auction based competitive procurement proposal is an open and transparent process that specifies in all material and relevant respects how the Companies will procure power and energy. The Ameren Companies have provided all their decision making criteria up-front and embodied that criteria in their tariff filing so as to effectively remove management discretion with respect to its procurement decisions. Although the running of an auction process may result in the independent Auction Manager taking certain actions that could be deemed discretionary, the basis upon which such determinations are to be made have been reasonably specified to the maximum extent possible. When these facts are considered, it is clear that the record in this proceeding supports the Companies' request for a prudence determination.

In addition, the Companies proposal provides for additional regulatory oversight in connection with the running of the auction itself. Under the Companies' proposal, Staff and such consulting expert or experts it selects will oversee all aspects of the auction process – including actions taken before, during and after the actual auction. This oversight will help ensure that the auction process is conducted appropriately, and that any potential problems are identified as early as possible and remedied. Moreover, Staff's oversight role will allow Staff and its experts to develop a sufficient knowledge base from which to report to the Commission on the conduct and outcome of the auction.

Moreover, in addition to the oversight of the auction process by Staff, the Companies' proposal allows the Commission to prevent implementation of the auction results by deciding to commence a formal proceeding within three days of the conclusion of an auction. Since all that needs to occur in this regard is a decision to commence a formal proceeding, the Commission is provided a broad and extensive tool with which to assure that the auction process proceeds as intended.

2. Post-auction Commission review of results

With respect to post-auction Commission review of results, see Staff discussion in Sections VII.K.1 and V.J.4 above. Staff reserves the right to respond in its rebuttal brief to other parties who address this matter in their initial briefs.

3. Post-auction workshop process

The Ameren Companies' proposed that the Commission convene workshops after each auction to evaluate the auction process and suggest improvements for the next auctions. (Resp. Ex. 4.0, pp. 13-14, lines 277-292)

IIEC witness Collins recommended that, instead of informal workshops, the Commission should hold formal proceedings to consider improvements to the auction process that should occur prior to the next auction, rather than afterwards as proposed by the Companies. (IIEC Exhibit 3.0. p. 16, lines 312-317) Specifically, Mr. Collins recommended that the Commission make a finding in this proceeding that the Commission will evaluate the fundamental structure of the auction process during the formal proceedings. (*Id.*, lines 330-331) In response, Ameren witness Mill noted that (with the exception of the time between the first and second auctions), there would be only about 5-6 months between auctions. Further, the Commission could open a formal docket at any time. (Resp. Ex. 16.0, pp. 10-11, lines 244-249 and 273-375)

Staff has no objection to the Companies' recommendation to establish informal workshops after the conclusion of the auction, rather than establish formal annual proceedings. The workshops, under Ameren's proposal, would be sponsored by the Commission, which should alleviate any concern that any party that wishes to comment on the conduct (and the results) of the auction would not have an opportunity to be heard in an open forum. While Staff understands that any tariff proposals that result from the workshops would likely be initiated by the Companies, rather than intervenors, parties would retain their rights to petition the Commission to open proceedings for the purpose of examining the Companies' tariffs or, in fact, for the purpose of evaluating the auction process itself.

4. Formal proceeding(s) to consider process

With respect to formal proceedings to consider the auction process, see the Staff discussion above in Section K.3. Staff reserves the right to respond in its reply brief to parties who that address this matter in their initial briefs

5. Other processes and proceedings

Staff will address in its reply brief any additional issues concerning other processes and proceedings that may be discussed by other parties.

L. Supplier forward contracts

1. Uniformity in general

As part of its filing in this proceeding, the Ameren Companies proposed supplier forward contracts ("SFCs"). ComEd also proposed its own SFCs in its procurement proceeding, Docket No. 05-0159, ("ComEd proceeding"). Staff witness Salant stated that "[b]oth sets of contracts should be designed to meet the same objectives, achieving the best outcome for ratepayers, one which balances near term costs and longer term default risks." (ICC Staff Exhibit 1.0, p. 111, lines 2523-2525) As originally proposed both contracts differed in many ways and, as a result, would increase bidder costs in reviewing and complying with the contracts and would reduce competition in each auction. (*Id.*, lines 2525-2534)

In his rebuttal testimony, Ameren witness Nelson recognized that "… there is substantial interest in greater uniformity between the Ameren Companies and ComEd in form and terms of the SFCs." (Resp. Ex. 10.0 Corrected, p. 6, lines 134-135) As a result, the Ameren Companies have worked with ComEd to achieve uniformity on all the aspects of the SFCs to the extent possible and proposed an amended contract. (*Id.*, p. 7, lines 141-143; Resp. Ex.11.0 Revised, p. 12, lines 262-271; and Resp. Ex. 11.1) Mr. Nelson also recommended that

> The Ameren Companies will present revised SFCs to the Commission as part of the record in this proceeding, and the Commission may, in its final Order, make findings concerning any work remaining, which can be satisfied in a compliance filing.

(Resp. Ex. 10.0, p. 7, lines 143-146)

Staff agrees with Mr. Nelson's suggestion for a compliance filing; however, it is Staff's position that the timing of such a filing should allow for an opportunity for consideration of supplier input. (ICC Staff Exhibit 11.0 Corrected, p. 21, lines 475-477) Since the Ameren Companies did not propose a timeframe for the compliance filing, Staff, in rebuttal testimony, recommended that the compliance filing due date be within sixty (60) days of the posting of the draft contract on the auction web site, which should occur within (7) days of the entry of the final order in this proceeding. (*Id.*, p. 22, lines 482-486) Staff further recommends that the Commission's order set forth additional details regarding the process for the compliance filing, such as identifying unresolved issues and directing the Ameren Companies, ComEd and the Auction Manager to file a petition with the Commission to resolve any open issues within 21 days of the compliance filing, with notice of such filing to the service list in Docket Nos. 05-0160/0161/0162 (Consol.). (*Id.*, lines 491-495)

Since they have met with ComEd and devoted substantial effort to harmonize the SFCs, the Ameren Companies believe the procedure set forth in the Auction timeline (Resp. Ex. 12.6) is sufficient. Mr. Blessing states as follows:

> In addition, I would like to point out that the Auction timeline does include a period of time for prospective bidders to submit comments regarding the SFCs. The process contemplates that first, should the proposed Auction process be approved in this docket, ComEd and Ameren would file SFCs with the ICC within ten (10) days of the ICC Order. ICC Staff would review the SFCs to ensure that they are fully compliant with the ICC Order, and at that point, the compliant SFCs would then be posted for prospective bidders. Bidders would then be invited to comment -- it being understood that no change could be made that would imperil the SFCs' compliance with the ICC Order. Bidder comments would be submitted to the Auction Manager and reviewed by the Auction Manager, ICC Staff, ComEd and the Ameren Companies. These parties would consult and would collectively consider the comments submitted and respond to prospective bidders. Comments reviewed by the Auction Manager, ICC Staff, ComEd and the Ameren Companies would then be incorporated to the extent that these parties agreed that they improved or clarified the document without jeopardizing compliance with the ICC Order.

(Resp. Ex. 18.0, pp. 14-15, lines 308-323)

Staff notes that Mr. Blessing states that bidders are "…invited to comment -- it being understood that no change could be made that would imperil the SFCs' compliance with the ICC Order." (*Id.*, p. 14, lines 314-316) That statement is unclear since it could be interpreted to mean that ComEd, Ameren, Staff or the Auction Manager could make changes that are inconsistent with the Commission's Order. Of course, such an interpretation would be improper as the final SFCs must be consistent with the ICC's Order.

Staff continues to recommend a 60-day compliance filing for finalizing the SFCs. A 60-day compliance filing would allow bidders time to provide comments regarding finalizing the SFCs and would also allow the Ameren Companies, ComEd, Staff and the Auction Manager time to consider, respond to and, if necessary, incorporate such comments into the final SFCs.

2. Credit requirements

Article 6 of Ameren's proposed SFCs describes the credit requirements. Staff witness Rochelle Phipps made three recommendations regarding the Ameren Companies' proposed credit requirements: (1) the level of the Ameren Companies' proposed credit requirements should be approved; (2) the provision to "notch" down issuer credit ratings by Moody's Investors Service should be eliminated; and (3) a reporting requirement for the Ameren Companies in connection with the credit provision that allows the Companies to unilaterally reduce their credit requirements should be established. (ICC Staff Exhibit 15.0, p. 2, lines 21-38) The only remaining contested issue relates to the credit provision that allows the Ameren Companies to unilaterally reduce their credit requirements, as described hereafter.

Ms. Phipps testified that the Ameren Companies have not shown that the proposed credit requirements are based on any quantitative analysis of their impact on auction prices or the degree of protection they provide ratepayers in the event of a supplier default. Ms. Phipps testified that this suggests the optimal credit requirements will only be determined through experience. Further, no party proposed alternative credit requirements. Thus, Staff recommends approval of the credit requirements provided in Article 6 of Ameren's SFCs. (ICC Staff Exhibit 15.0, p. 2, lines 28-38)

Ms. Phipps also testified that the Ameren Companies' proposed credit requirements and those proposed by ComEd in the ComEd proceeding are more alike than different, with the difference being in the amount of the dollar caps. Given the similarity between the Ameren Companies' and ComEd's proposed credit requirements and the fact that the optimal level of credit requirements is unknown at this point in time, Ms. Phipps did not object to the Ameren Companies' proposed credit requirements differing from those proposed in the ComEd proceeding. (ICC Staff Exhibit 15.0, p. 8, lines 157-175)

Staff witness Phipps also recommended eliminating the credit provision in the Ameren Companies' proposed SFCs that requires "notching down" the corporate issuer credit rating from Moody's Investors Service ("Moody's") because Moody's issuer ratings are already equivalent to unsecured credit ratings. (ICC Staff Exhibit 15.0, p. 6, lines 144-147) The Companies agreed to modify their SFCs to eliminate notching

Moody's issuer credit ratings in Sections 6.4 and 6.8a of their proposed SFCs. (Resp. Ex. 21.0, p. 3, lines 51-56)

Finally, Section 6.1 of the Ameren Companies' proposed SFCs initially allowed the Companies to unilaterally reduce the credit requirements, which provided them the flexibility to respond to "significant, unforeseen circumstances … [in order] to accomplish objectives such as ensuring reliability, dampening price volatility and maintaining market stability". Ms. Phipps testified that since there is no basis to currently assess the reasonableness of unspecified future changes in credit requirements, the Commission should retain the ability to review any such changes after the fact if they do occur. (ICC Staff Exhibit 15.0, p. 3, lines 44-60) Thus, Ms. Phipps recommended that should the Ameren Companies change the SFC credit requirements, within 15 days of the changes in credit requirements, they file a report with the Manager of the Commission's Finance Department and Chief Clerk that identifies the effective date, explains the reason for the change and summarizes any facts and analyses on which the decision to change the credit requirements was based. (ICC Staff Exhibit 15.0, p. 4, lines 64-70) Ms. Phipps also recommended the Ameren Companies clarify whether the SFCs permit Ameren to restore the credit requirements to their initial level as circumstances permit. (ICC Staff Exhibit 15.0, p. 3, lines 61-63)

In response to Ms. Phipps' proposed reporting requirement, Ameren witness Timothy Moloney proposed eliminating the credit provision from Section 6.1 of the SFCs that allows the Company to unilaterally reduce its credit requirements. He asserted that the Ameren Companies believe that a review by the Commission or Staff would be acceptable in advance of implementing changes to the credit requirements. (Resp. Ex.

21.0, pp. 2-3, lines 45-48) Staff objects to the proposal to eliminate this credit provision. Staff found the Ameren Companies' argument for including this credit provision convincing and believes that the flexibility provided by this credit provision could potentially benefit both customers and suppliers. Moreover, the Companies have not provided any details regarding its proposal to confer with the Commission or Staff before reducing the credit requirements. Specifically, the Ameren Companies have not specified (1) the proposed procedure for discussing with the Commission or Commission Staff any proposal to reduce the SFC credit requirements; (2) the information the Ameren Companies would provide the Commission or Staff should they seek to establish less restrictive credit requirements; (3) the amount of time the Commission or Commission Staff would have to review any proposed reduction in credit requirements; and (4) any input the Ameren Companies would seek from the Commission or Staff during the time allotted for review of any proposed reduction in credit requirements. (ICC Staff Cross Exhibit 8) Staff believes it would be unwise to rely on a process with so many unknown variables. Thus, the Ameren Companies' proposal to eliminate the credit provision allowing them to unilaterally reduce their credit requirements should be rejected. In other words, the credit provision should remain in Section 6.1 of the SFCs and Ms. Phipps' proposed reporting requirement in connection with this credit provision should be adopted. Moreover, the Ameren Companies should be required to revise their SFCs to clarify that following any reduction in credit ratings pursuant to Section 6.1 of the SFCs, the Ameren Companies may restore the credit requirements to their initial level as circumstances permit.

3. Proposed clarifications and modifications accepted by Ameren

As described in Section V.L.2., Ameren agreed to modify its SFCs to eliminate notching Moody's issuer credit ratings. (Resp. Ex. 21.0, p. 3, lines 55-56)

Staff witness Dr. Salant testified that Section 6.8 of the Ameren Companies' proposed SFCs does not provide protection against non-payment for delivered power if the credit rating of only one of the three Ameren companies falls below investment grade. (ICC Staff Exhibit 1.0, p. 109, lines 2492-2495) Thus, he recommended revising Section 6.8 to allow transferring the supplier's margin to a Qualified Institution (as defined in the SFCs) in the event the credit rating of one or more of the Ameren companies falls below investment grade. (ICC Staff Exhibit 1.0, p. 110, lines 2497-2502) The Ameren Companies agreed to modify the provision in Section 6.8 in accordance with Dr. Salant's recommendation. That is, if the credit rating of one of the Ameren companies falls below investment grade, then the amount of collateral held related to the level of exposure that such downgraded Ameren company has to a supplier will be transferred to a Qualified Institution upon receipt of written request from the supplier whereas collateral held by Ameren companies with investment grade ratings may continue to be held by them at their discretion. (Resp. Ex. 14.0, p. 8, lines 172-178)

Dr. Salant also testified that when the ratings of any two of the Ameren companies falls below investment grade, Section 9.1 provides the supplier with the remedy of negotiating for an acceleration of the payment schedule with all three Ameren companies, which is of little value to suppliers because that remedy is neither immediate nor self-executing. Thus, Dr. Salant recommended revising Section 9.1 to allow a supplier to take action to protect itself against a defaulting utility when the credit rating of one or more of the Ameren companies falls below investment grade. He recommended further that Ameren should include provisions that are both immediate and self-executing in the event one or more of its utility affiliates fall below investment grade. (ICC Staff Exhibit 1.0, p. 110, lines 2505-2518) Ameren witness Moloney testified that the Ameren Companies will modify Section 9 so that in the event the credit rating of one or more of the Ameren companies were to fall below investment grade, the payments due from such downgraded Ameren company would automatically be accelerated to twice per month whereas payments due from the Ameren companies that carry investment grade ratings will continue to be made on a monthly basis. (Resp. Ex. 14.0, p. 9, lines 186-190)

Finally, Dr. Salant asked the Ameren Companies to explain why they did not include a provision in its SFCs that requires notifying suppliers in the event the rating of an Ameren company is downgraded below investment grade. (ICC Staff Exhibit 1.0, p. 113, lines 2565-2567) In response, the Ameren Companies agreed to modify the SFCs by requiring the Ameren Companies to provide prompt notification to the suppliers in the event that any Ameren company should fall below investment grade. (Resp. Ex. 14.0, p. 8, lines 162-164)

4. Proposed clarifications and modifications not accepted by Ameren

a. Compliance Filing

As stated in section V.L.1, Staff recommends a 60-day compliance filing in connection with finalizing the SFCs, which would allow bidders time to provide comments regarding finalizing the SFCs and would also allow the Ameren Companies, ComEd, Staff and the Auction Manager time to consider, respond to and, if necessary, incorporate such comments into the final SFCs.

b. Credit Requirements

As described in Section V.L.2., the Ameren Companies ultimately proposed eliminating the credit provision from Section 6.1 of the SFCs that allows the Companies to unilaterally reduce their credit requirements. (Resp. Ex. 17.0, p. 3, lines 48-50) For the reasons described previously, the Ameren Companies' proposal should be rejected. That is, the credit provision allowing the Ameren Companies to unilaterally reduce their credit requirements should remain in Section 6.1 of the SFCs and Ms. Phipps' proposed reporting requirement in connection with this credit provision should be adopted.

c. Force Majeure

As originally filed, Section 2.1.b.(v) of the Ameren Companies SFC stated:

> Except for the circumstance in which physical impossibility, not due to any gross negligence or willful misconduct of the BGS-FP Supplier, prevents the delivery of Energy to a Delivery Point : (a) the BGS-FP Supplier's obligation to deliver Energy to such Delivery Point pursuant to this Agreement shall be absolute and unconditional and shall not be affected by any circumstances of any character, (b) the BGS-FP Supplier has assumed full, complete and sole responsibility, without reservation or condition, for the delivery of Energy to such Delivery Point pursuant to this Agreement, and (c) it is the intention of the Parties that no event or condition (whether foreseen or unforeseen and whether such event or condition might otherwise serve as a defense or relieve the BGS-FP Supplier of its obligations and liabilities hereunder) shall excuse the BGS-FP Supplier's performance pursuant to this Agreement . A lack of Energy offered in any LMP Market (forward or real-time) does not constitute a physical impossibility, as that term is used in the foregoing sentence.

(Resp. Ex. 3.1, 3.2 and 3.3) This section of the SFCs refers to circumstances beyond a supplier's control that may make it impossible for the supplier to deliver the contracted supply, otherwise known as Force Majeure. (ICC Staff Exhibit 1.0, p. 104, lines 2369-2372) Unlike the provision proposed by ComEd in its SFCs filed as part of its procurement proceeding (Docket No. 05-0159), the Ameren Companies' provision -- while providing the supplier with the option of arranging alternative delivery -- appeared to invalidate the application of a defense of Force Majeure. (*Id.*, p. 105, lines 2393-2398) It appeared that Ameren wanted a "supplier to retain responsibility for meeting the load requirements except when energy cannot be delivered." (Id., p. 19, lines 413-416) Thus, Staff recommended that the Ameren Companies adopt the ComEd Force Majeure provision as it more clearly captured this intent. (*Id.*, lines 416-419)

Ameren witness Blessing responded to Staff's concern by testifying that the Ameren Companies will adopt ComEd's Force Majeure language:

> … with the exception that the Ameren Companies continue to exclude the unavailability of Energy in the LMP markets from the circumstances providing Force Majeure relief to suppliers.

(Resp. Ex. 18.0, p. 2, lines 41-44) The Companies' adoption of the Force Majeure language utilized by ComEd provides additional clarity. Staff does not believe that the Ameren Companies' limited addition to that language detracts from that clarity to any significant extent, and therefore does not object to the Ameren Companies' exception. Therefore, Staff recommends that the Commission adopt the amended Force Majeure provision as reflected in Resp. Exhibit 18.1.

d. Joint and Several Liability

Under the SFCs proposed by the Ameren Companies, each contract will contain multiple purchasers (*i.e.*, AmerenCIPS, AmerenCILCO and AmerenIP) and a single seller (*i.e.*, a successful bidder for one or more tranches). This multi-party purchaser structure necessarily raises the issue of whether each of the Ameren Companies will have "joint and several" contractual obligations or only "several" obligations. In Brokerage Resources, Inc. v. Jordan, 80 Ill. App. 3d 605, 608-609 (1st Dist. 1980) the Court described the general framework under Illinois law[11] for determining whether a contract results in joint and several obligations, and explained the general effect of having joint and several obligations or covenants:

> In Illinois, joint contractual obligations generally "shall be taken and held to be joint and several obligations and covenants." (Ill. Rev. Stat. 1977, ch. 76, par. 3. [now 765 ILCS 1005/3]) Whether a contractual obligation is joint and several, or only several, depends upon the intentions of the parties, as revealed by the language of the contract and the subject matter to which it relates. (*Filosa v. Pecora (1974), 18 Ill. App. 3d 123, 309 N.E.2d 356; 17 Am. Jur. 2d Contracts § § 298-300* (1964).) Parties to a contract are more likely to have a joint and several contractual obligation if they have a joint or identical interest in the contract or its subject matter, instead of diverse interests. (*17 Am. Jur. 2d Contracts § § 298-300* (1964).) If two or more parties to a contract owe a joint and several duty of performance to another party to the contract and the duty is not performed, each may be liable for the entire damages resulting from the failure to perform. (See *Pleasure Driveway & Park District v. Jones (1977), 5 Ill. App. 3d 182, 367 N.E.2d 111;* 23A Ill. L. & Prac. *Judgments* § 382 (1979); *17 Am. Jur. 2d Contracts § § 298-300* (1964).) As stated in Illinois Law & Practice (12 Ill. L. & Prac. *Contracts* § 263 (1955)), [w]here the promise of several is both joint and several, the contract is in legal contemplation double, that is, equivalent to independent contracts founded on one consideration, for performance

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[11] The SFCs provide that "[e]xcept to the extent that the FPA governs questions, including those concerning the formation, validity, interpretation, execution, amendment, termination and construction of this Agreement, shall be governed by the laws of the State of Illinois, without regard to principles of conflicts of law." (See Resp. Ex. 18.1 (Revised), p. 66, § 15.4)

> severally, and also for performance jointly, and distinct remedies on the same instrument, treating it as a joint and several contract, may be pursued until full satisfaction is obtained." In addition, if a party to a contract is held liable for the entire damages resulting from the breach of a joint and several contractual obligation, that party is not being held to answer for what is exclusively the debt of another, but is being held responsible for an obligation which is his directly due to the joint and several nature of the obligation. In such a situation, section 1 of the Statute of Frauds' requirement of a signed writing containing a "special promise to answer for the debt, default or miscarriage of another person" is inapplicable. See *Baker Farmers Co. v. ASF Corp. (1975), 28 Ill. App. 3d 393, 328 N.E.2d 369.*

(*Id.*)

Staff witness Dr. Salant explained that the multi-party purchaser provision of the SFCs gives rise to several concerns with respect to the Ameren Companies' auction proposal:

> The multiple-party purchaser provision is a concern because the relationship among the utilities, particularly with respect to whether liability is joint or individual, is ambiguous. Notwithstanding §15.13(ii) of the proposed group of contracts which disclaims joint and several liability to the supplier, ambiguity arises because the rights and obligations of the Companies are not individualized and are not specified in the event that one or more of the Companies defaults under the agreement. Since the contract is not clear with respect to the status of the contract itself in the event of a default by one Company, there is uncertainty for both supplier and the Companies. For example, if one Company defaulted by not making a timely monthly payment for supply received, while the other two Companies did make timely payment, §5.2 allows the supplier to terminate the contract, or accelerate all amounts owning "between" (another indication of joint liability) the Parties, or to suspend performance under the Agreement, or all or any combination of the above. What is implied, but not made clear, is whether the action applies to all three Ameren Companies or can apply just to the defaulting party. Thus, the two non-defaulting utilities' supply may be contingent upon all three Companies performing their obligations in a timely manner. If uncertainty with respect to supply and the price of that supply is intended and acceptable to the ratepayers, then such risks should be unambiguous, and those accepting the risks on behalf of the ratepayers should be clear about the risks being accepted.
>
> It may be the case that the likelihood of default by one of the utilities is remote. However, as the recent experience with Pacific Gas and Electric

> in California demonstrates, events that were thought to be too unlikely to consider can occur. Companies with A credit ratings may default on payments to suppliers under certain circumstances. The lack of clarity with respect to the relationship among the three Ameren companies heightens the credit risk accepted by the suppliers.

(Staff Exhibit 1.0, pp. 106-107, lines 2415-2444) Staff witness Dr. Salant recommended that the SFCs be re-drafted to clearly define the consequences of default by one of the Ameren Companies since the removal of that uncertainty would be consistent with the goal "to produce an auction with the lowest possible prices . . . ." (*Id.*, p. 108, lines 2449-2453)

In rebuttal, Ameren witness Blessing disagreed with Dr. Salant's recommendation that the Ameren Companies re-draft the SFCs to clarify the consequences of default by one of the Ameren Companies. (Resp. Ex. 11.0 (Revised), p. 14, lines 299-318) Mr. Blessing took the position that no clarification was necessary because the language of the SFCs provides that "the Ameren Companies shall not be jointly and severally liable to the BGS Supplier . . . ." (*Id.*) Mr. Blessing further contended that:

> Article 5 is unambiguous in providing that a default by any of the Ameren Companies in respect of a material obligation owed to the BGS Supplier would render the BGS Supplier the "Non-Defaulting Party" and would entitle it to any of the rights and remedies provided upon the occurrence of an Event of Default. Again, the definition of "Non-Defaulting Party" is unambiguous on this point; if any of the Ameren Companies is the Defaulting Party, then the BGS Supplier is the Non-Defaulting Party and it may exercise any of the rights and remedies provided in Section 5.2.

(*Id.*) Mr. Blessing's assertion only serves to add to the ambiguity of Ameren's proposed SFCs concerning joint and several obligations. As Mr. Blessing notes, under the language of the SFCs (see Resp. Ex. 11.1 and Resp. Ex. 11.2) a default by **any** one of the Ameren Companies provides the BGS Supplier with all the rights and remedies provided in Section 5.2. One of those rights is the right to terminate the SFC by establishment of an Early Termination Date. (Resp. Ex. 11.1 and Resp. Ex. 11.2, Sections 4.1a and 5.2) Thus, although Mr. Blessing contends that the obligations of each of the Ameren Companies are separate and distinct under the SFCs, he also acknowledges that the wording of the Ameren Companies' proposed SFCs would allow a default by one of the Ameren Companies to result in a termination of the SFC for the other two non-defaulting Ameren Companies.

In Staff's rebuttal testimony filing, Dr. Salant described inconsistencies between (i) Mr. Blessing's assertion that the SFCs set forth individual obligations for each of the Ameren Companies and (ii) specific language in the SFCs setting forth rights and obligations of the Ameren Companies on a collective basis. (ICC Staff Exhibit 11.0 Corrected, pp. 19-20, lines 421-451) Dr. Salant again recommended that the various provisions contained within the SFCs be re-drafted to make clear "whether the contract is referring to the Companies collectively or whether each Company has a separate obligation." Although Dr. Salant's preference was for the SFCs to be re-drafted with the three Ameren Companies jointly and severally liable to the BGS Supplier; his alternative recommendation (*i.e.*, in the event that joint and several obligations were not possible) was for the SFCs to be re-drafted to provide separate contracts or sub-agreements that "(i) include separate payment provisions for each utility, (ii) separate the other obligations of the utilities, and (iii) completely describe the termination and default provisions if only one or two of the three Ameren Companies default or terminate the contract." (*Id.*, pp. 20-21, lines 452-466)

Ameren submitted a revised form of SFC through the surrebuttal testimony of Ameren witness Blessing. (See Resp. Ex. 18.0, pp. 2-3, lines 32-67; Resp. Ex. 18.1; Resp. Ex. 18.2) The revised form SFC contained various organizational and substantive modifications, including revisions to make the Ameren Companies' proposed SFCs more closely conform to the comparable ComEd contracts. (*Id.*) With respect to Dr. Salant's recommendation to re-draft the SFCs to provide for joint and several liability, Mr. Blessing explained that such an action was not feasible:

> … the Ameren Companies cannot undertake to commit themselves to assuming joint and several liability to the BGS Suppliers because they are not authorized by the ICC to pay or guarantee each others' debt or obligations. We have not sought to obtain such authorization from the ICC, nor do we believe that seeking such authorization would advance the objectives of this proceeding.

(Resp. Ex. 18.0, p. 6, lines 122-127)

Staff notes that Section 7-102(A)(f) of the Public Utilities Act provides that "[n]o public utility may in any manner, directly or indirectly, guarantee the performance of any contract or other obligation of any other person, firm or corporation whatsoever" without first obtaining the consent and approval of the Commission. (220 ILCS 5/7-102(A)(f)) No such approval has been sought or obtained in the instant case. As a result, Staff does not dispute that it would be impermissible for the SFCs to contain provisions directly or indirectly amounting to a guarantee by the individual Ameren Companies of each others' obligations under the SFCs.

This then leaves Dr. Salant's alternative recommendation for Ameren to re-draft the SFCs to clearly specify the separate obligations of each of the Ameren Companies. Although Mr. Blessing did not directly address Dr. Salant's alternative recommendation in the question and answer portion of his surrebuttal testimony, he did attach to his testimony clean (Resp. Ex. 18.1) and redlined (Resp. Ex. 18.2) versions of the revised form SFC -- and the revisions disclosed therein reveal that the Ameren Companies did revise the form SFC to more clearly delineate the separate and independent obligations of the Ameren Companies (*i.e.*, not joint and several) under the SFCs. (Resp. Ex. 18.0, p. 3, lines 62-67; Resp. Ex. 18.1, Resp. Ex. 18.2) The relevant changes made to the form SFC include the following:

- Added item (x) of Section 1.3 which provides that "reference to 'termination of this Agreement,' 'this Agreement is terminated,' 'this Agreement may be terminated' and similar phrases used in this Agreement refer to the termination of deliveries under this Agreement and related on-going rights and obligations, and does not imply or mean a termination of rights, remedies, obligations and provisions which by their nature or as provided elsewhere in the Agreement survive termination." (Resp. Ex. 18.2, p. 20) This language makes clear that references to termination of the agreement can refer to the termination of specific obligations rather than the termination of the whole agreement.

- Changes the language setting forth the obligations of the companies from "The Companies hereby agree as follows" to "Each of the Companies hereby agrees as follows". (*Id.*, p. 25) Additionally, the introductory language for each paragraph setting forth specific obligations was revised from "The Companies will" to "The Company will". (*Id.*, pp. 25-27) Similar changes were made with respect to the Representations, Warranties and Covenants language. (*Id.*, pp. 32-34) These changes are clearly consistent with individual obligations rather than collective obligations. Staff notes that there are a few instances in the sample form SFC (for example, Section 5.1 Events of Default) where there are references to "the Companies" instead of "each of the Companies". Staff assumes that such omissions were inadvertent, and anticipates that the final version of the SFCs to be utilized in connection with the auction will be revised in a similar manner. (See *Id.*, p. 39)

- Adds language to the section regarding Rights Upon Default to specify that the right to elect an Early Termination Date is "with respect to the obligations of the Defaulting Party". (*Id.*, p. 41) Thus, with this modification, the election of Early Termination upon the default of less than all of the Ameren Companies would only result in the termination of the agreement with respect to the obligations of the defaulting Ameren Companies.

The above-described revisions indicate (i) that the Ameren Companies clearly intend for the form SFC to state separate and independent obligations for each of the Ameren Companies (*i.e.*, not joint and several) and (ii) that the language of the revised form SFC is substantially consistent with and reflects that intent. As noted above, additional clarity would be obtained if most or all of the remaining references to "the Companies" were changed to "each of the Companies" to further reflect the independent nature of the referenced rights or obligations. Further, Staff believes that additional clarity would be obtained if a sentence were added to paragraph (ii) of "Section 5.2 Rights Upon Default" as follows: "In the event that a Non-Defaulting Party elects to designate an Early Termination Date with respect to the obligations of a Defaulting Party, the rights, liabilities, powers and obligations of any other Non-Defaulting Parties shall survive such termination."

As noted above, the revised form SFC contains a provision indicating that references to termination do not infer or imply termination of "rights, remedies, obligations and provisions which by their nature or as provided elsewhere in the Agreement survive termination." (Resp. Ex. 18.2, p. 20) Similarly, a provision was added specifying that "[c]ancellation, expiration or termination, including Early Termination, of this Agreement shall not terminate provisions, rights, liabilities, powers and obligations under or afforded by this Agreement that (a) by their nature or **express terms** survive such cancellation, expiration or termination" (*Id.*, p. 79 (emphasis added) The sentence proposed above simply makes survival of the rights and obligations of non-defaulting parties in the event of a default by less than all of the Ameren

Companies an "express term" of the SFC, thereby removing any potential dispute or ambiguity regarding this intent.

There is one other provision of the revised form SFC that should be discussed in connection with the termination provisions. Mr. Blessing indicates in his surrebuttal testimony that one modification to the form SFC was as follow:

> We have now provided that the termination of any one of multiple contracts between a Supplier and one of the Ameren Companies for BGS Supply results in the automatic termination of all such contracts between that Supplier and the Ameren Companies. See SFC Section 5.4.e.

(Resp. Ex. 18.0, pp. 2-3, lines 45-49; see also Resp. Ex. 18.2, p. 46, Section 5.4.e) This language should be clarified to make clear that such "automatic termination" shall only apply with respect to the obligations of the Defaulting Party in the event that such termination involves a default by fewer than all of the Ameren Companies.

For all the foregoing reasons, the Commission should direct the Ameren Companies to further revise the form SFCs to: (1) change remaining references to "the Companies" to "each of the Companies" to reflect the independent nature of the referenced rights or obligations; (2) add a sentence to paragraph (ii) of "Section 5.2 Rights Upon Default" providing that the rights and obligations of Non-Defaulting Parties survive an Early Termination applicable to one Defaulting Party in the event of a default by less than all of the Ameren Companies; and (3) clarify the language of Section 5.4.e to express that an "automatic termination" shall only apply with respect to the obligations of the Defaulting Party in the event that such termination involves a default by fewer than all of the Ameren Companies.

e. Procurement of Ancillary Services

In their initial filing, the Ameren Companies proposed that they be responsible for the procurement of ancillary services from the MISO with the costs of such ancillary services to be passed on to the suppliers. (Resp. Ex. 3.0, pp. 14-15, lines 302-315; Resp. Ex. 3.1, p. 22, Section 2.1.c.(iii)) Staff witness Ogur recommended in his direct testimony that "the pro-forma contracts be modified to give the suppliers the additional option of self-supplying or self-procuring their shares of ancillary services." (ICC Staff Exhibit 4.0, p. 28, lines 595-598) Mr. Ogur had three reasons for his recommendation. First, "there are no costs associated with this additional option." (*Id.*, p. 27, line 582) A supplier can decline this option and have the Companies procure its share of ancillary services from MISO. Further, the Companies incur no costs because they can pass on to the supplier exactly the amount MISO charges the Companies for ancillary services. (*Id.*, p. 27, lines 582-587)

Second, offering such option for procurement of ancillary services may result in two benefits: (1) an increase in auction participation or (2) lower price bids by bidders due to lower expected ancillary services procurement costs or higher certainty about such costs. Accordingly, offering such an option may potentially lower auction prices and thus lower rates for end use customers. (*Id.*, p. 27, lines 587-592)

Third, the MISO Tariff has explicit provisions that would allow the Ameren Companies to give suppliers the option of self-procuring ancillary services. Further, Staff witness Ogur testified that there are at least two distinct ways that this could be achieved while the Companies satisfy their requirements as Transmission Customers. (*Id.*, pp. 24-26, lines 525-550)

In his rebuttal testimony, Ameren Witness Blessing disagreed with Mr. Ogur's recommendation that the suppliers be given the option to self-supply ancillary services. (Resp. Ex. 11.0 (Revised), pp. 43-48) In support of his position, Mr. Blessing testified that providing an option to self-supply ancillary services could provide a BGS supplier an undue advantage because certain costs for arranging the self-supply of ancillary services are not easily identifiable or assignable to particular parties. (Resp. Ex. 11.0 (Revised), lines 1060-1066). He added that self-supply of ancillary services is complex and costly. He further found self-supply particularly problematic because (1) the subject loads must be metered in real time and currently, such meters are not in place, and (2) the BGS supplier's response must be measurable by and visible to the control area. (*Id.*, p. 45, lines 1003-1011) Mr. Blessing also testifies that considering the expected development of MISO's ancillary services market in 2006-2007, Mr. Ogur's concern is somewhat transitional in nature. (*Id.*, p. 44, lines 990-993) Finally, he states that the cost of ancillary services make a relatively small contribution to the total expected cost of supply. (*Id.*, pp. 47-48, lines 1068-1080)

In his rebuttal testimony, Staff witness Ogur disagreed with Mr. Blessing's stated reasons for opposing the option allowing bidders to self-supply ancillary services. Mr. Ogur rejected Mr. Blessing's rebuttal testimony on several grounds.

First, Mr. Blessing's argument that a supplier may receive an unwarranted competitive advantage through providing such a self-supply option is vague at best. Mr. Blessing merely states that "there may be certain costs which are not easily identifiable or assignable to particular parties" without even providing an example of such costs. A possibility that a supplier may gain an unwarranted competitive advantage, which is neither qualified nor quantified, is not a sound basis to deny suppliers a legitimate option. (ICC Staff Exhibit 19.0, p. 5, lines 88-95)

Also, the assertion that certain costs for arranging self-supply of ancillary services are not easily identifiable or assignable to particular parties and could lead to an unwarranted competitive advantage is a potential problem that is neither unique nor limited to the Illinois procurement auction. However, despite this "problem", the option to self-supply is an option that any transmission customer has under the MISO Tariff. If this option were problematic, it would not have been approved by the Federal Energy Regulatory Commission as just and reasonable as part of the MISO Tariff. (*Id.*, pp. 5-6, lines 96-109) Finally, since it is the duty of the Ameren Companies, as MISO control area operators, to identify, quantify and assign such costs to market participants, such cost discrepancies will not arise to the extent the Companies fulfill this function. (*Id.*, p. 6, lines 110-114)

Second, the argument that self-supply of ancillary services is complex and costly only applies to one of the three ancillary services that can be self-supplied under the MISO Tariff. As Staff witness Ogur testified:

> Mr. Blessing discusses difficulties of self-supplying regulation service (Schedule 3); however, he does not advance any arguments to suggest that self-supply of the other two ancillary services, spinning reserve (Schedule 5) and supplemental reserve (Schedule 6), is complex, costly or impossible. Therefore, even if one were to accept for purposes of argument only everything Mr. Blessing states in his rebuttal testimony concerning regulation service, there would still be no reason to deny suppliers the option of self-supplying Schedule 5 and Schedule 6 ancillary services."

(ICC Staff Exhibit 19.0, pp. 7-8, lines 142-152)

As part of his argument that allowing bidders an option to self-supply ancillary services would be complex and costly, Mr. Blessing stated that "the subject loads must be metered in real time so as to allow the individual contribution of each BGS Supplier to the required regulation action be calculated and transmitted in real time." (Resp. Ex. 11.0 (Revised), p. 45, lines 1007-1010) Staff notes that Mr. Blessing fails to cite any MISO source for his statement. (ICC Staff Exhibit 19.0, p. 8, lines 153-157) Further, even if the Ameren load tranches in the auction are ineligible for self-supply of ancillary services under the MISO Tariff, then this option would automatically be void because the Ameren Companies' SFCs make supplier performance subject to MISO rules and procedures (Resp. Ex. 3.1, p. 19, Section 2.1.a.(vi)). (ICC Staff Exhibit 19.0, p. 9, lines 171-182)

Further, whether the self-supply of ancillary services is "quite complex and costly" is simply not relevant. As Staff witness Ogur testified, what is relevant is whether it is feasible for suppliers to self-supply ancillary services. He further testified that

> It is established that under some circumstances, it is feasible to allow a supplier to self-supply ancillary services. Since the supplier will have to bear all the costs to comply with the MISO requirements, it is irrelevant how high those costs are. If the costs are more than the benefits, no supplier will choose to self-supply ancillary services. Thus, there can be no adverse consequence of giving this option to the suppliers, as the suppliers will conveniently refuse to utilize it."

(*Id.*, pp. 9-10, lines 188-194)

Mr. Blessing's argument that Staff's recommendation is transitional in nature due to the expected development of MISO's ancillary services market is no longer realistic due to the recent developments in MISO, as detailed in Mr. Ogur's rebuttal testimony. (*Id.*, pp. 11-13) Further, even if Staff's recommendation were truly transitional and the transition time were as short as Ameren witnesses McNamara and Blessing indicate, the Companies still have forwarded no rationale for denying the suppliers a legitimate option for self-supply of ancillary services, considering its potentially beneficial impacts on the participation in the auction and the resulting auction prices. (*Id.*, p. 13, lines 276-281) As stated by Staff witness Ogur,

> If the net benefits of an option outweigh its costs, that option should be implemented regardless of the time frame."

(*Id.*, p. 13, lines 281-282)

Finally, given the fact that providing this option to the suppliers costs nothing to the Ameren Companies or their ratepayers, from a policy making perspective, it would be unwise to exclude such an option, regardless of how the size of its benefits are qualified. (*Id.*, p. 15, lines 309-312) Further, if the potential benefits indeed are not large enough to justify allowing this option to the suppliers and no supplier will be interested in using this option, then no harm results in offering this option since it is unlikely a supplier would utilize it. (*Id.*, lines 313-317) Also, Staff further notes that Mr. Blessing's claim about the insignificance of the potential benefits is contradictory to his statement that a supplier can gain an "unwarranted competitive advantage" in the process of self-supplying ancillary services. If such benefits are so insignificant, then those benefits should not be a significant source of unwarranted competitive advantage to a supplier. (*Id.*, lines 317-324)

In surrebuttal testimony, Mr. Blessing continued to disagree with Mr. Ogur's position and recommended that the suppliers not be given the option of self-supplying ancillary services. (Resp. Ex. 18.0, p. 37) Mr. Blessing concluded that Mr. Ogur's recommendation is not warranted based on the following reasons:

a. Self-supply of Schedule 3 (regulation service) is accomplished by the establishment of a pseudo-tie, which requires real-time metering, as indicated in Section 5.4 of MISO's Business Practices Manual for Coordinated Reliability, Dispatch, & Control. (*Id.*, p. 33, lines 741-748)

b. It is unlikely that including provisions for self-supply of ancillary services in the SFCs will result in the benefits for customers that Mr. Ogur envisions. Also, Mr. Ogur's proposal may result in disagreement, ill will, and possibly litigation. (*Id.*, p. 35, lines 751-754)

c. The administrative effort and risk exposure incurred by the Ameren Companies as Transmission Customers and Load Serving Entities is not necessarily commensurate with that which is related to having the Ameren Companies directly acquire the ancillary services for all supplies and pass through the applicable charges to individual Suppliers. (*Id.*, p. 36, lines 801-807)

d. It is unsound to tie developments in the capacity markets to developments of ancillary services markets. "The Ancillary Service Task Force at MISO is actively working on this issue and the MISO's proposed 2006 capital budget which is currently under consideration includes a specific project (0209-06) for market enhancements related to Ancillary Services." (*Id.*, pp. 36-37, lines 815-820)

Moreover, Mr. Blessing proposes conditions he believes the Commission should impose if the Commission were to order the inclusion of the option of self-supply of ancillary services for the suppliers in the SFCs:

> If, however, the ICC were to determine that it would be appropriate to include such a provision in the SFC, it would be critical that such a provision clearly indicate that the provision of such resources must comply with all applicable Transmission Service Provider tariff requirements and the requirements of the applicable Balancing Authority, and that such a contract provision does not infer or otherwise suggest that the Supplier's proposed arrangements will be acceptable to Transmission Service Provider or the Balancing Authority. Further, such arrangements would need to be in place prior to the earlier of commencement of service or such time that the Ameren Companies as the Transmission Service Customer would be required to make an election of the method of procuring ancillary services to MISO. Finally, provisions related to the recovery of MISO charges and other incremental costs incurred by the Ameren Companies to accommodate such an option would need to be included in the SFC, to ensure that the Supplier incurs to the greatest extent possible the full and complete cost of electing such an option.

(*Id.*, p. 37, lines 826-840)

With respect to whether real-time metering is required for self-supply of ancillary services and whether after-the-fact metering is a legitimate way of self-supplying ancillary services, Staff witness Ogur stated during cross examination:

> Q. Referring to lines 165 to 167 of your rebuttal testimony, go ahead and get that. Can you identify any provision of the MISO energy market tariff or business practices which would allow for providing ancillary services on an estimated basis with later true-up?
>
> A. Yes.
>
> Q. Can you tell me what section that is?
>
> A. This would be Business Practices Manual, MISO Coordinated Reliability Dispatch and Control, Business Practices Manual of MISO, pages 5-12 and 5-13. When it discusses pseudo-ties, it identifies pseudo-ties as -- forming pseudo-ties as one of the ways to implement these transfers. But it also implies that it is not the only way to do it. For example, at the beginning of Section 5.4 it states "absent pre-existing agreements where metering and telemetry are already addressed between the attaining and native balancing authorities, pseudo-ties are established and have appropriate real time tie-line quality metering installed at all points," etc. So if there are pre-existing agreements for metering and telemetry already addressed between attaining and native balancing authorities, pseudo-ties are not necessary. Therefore, real time metering is not necessary.
>
> Q. And that specifically allows for providing ancillary services on an estimated basis with later true-up?
>
> A. It doesn't exclude it.
>
> Q. But it doesn't specifically offer it either, does it?
>
> A. On page 5-13 of the same document it states hourly schedules or load forecasts, as well as after-the-fact metering may be required if the native balancing authority is supplying any of the ancillary services. Therefore, yes, it does allow for that, on a load forecast basis as opposed to a real time metering basis.

(<u>Corrected</u> Common Tr., p. 21, line 15 - p. 23, line 9)

Thus, based on the foregoing, it is worthwhile to make some observations about the evidence in the record.

First, the Companies never responded to Staff witness Ogur's claim that the record was devoid of evidence suggesting that there is any difficulty or impossibility associated with giving the suppliers the option of self-supplying two of the ancillary services, spinning reserve (Schedule 5) and supplemental reserve (Schedule 6). Thus, Staff's position on self-supply of Schedule 5 and Schedule 6 ancillary services should be accepted.

Second, despite Ameren witness Blessing's "understanding" that real-time metering is required for self-supply of regulation service, Mr. Ogur's cross examination (the relevant part of which is quoted above) revealed that there is no such requirement. Section 5.4 of the Coordinated Reliability, Dispatch, & Control Business Practices Manual of MISO clearly and explicitly states that hourly schedules, load forecasts as well as after-the-fact metering may be utilized. Therefore, the Companies' alleged impediment to implementation of regulation service self-supply option for the suppliers is not valid.

Third, the Companies never satisfactorily responded to Mr. Ogur's arguments that (i) Ameren witness Blessing's argument that "certain costs which are not easily identifiable or assignable" associated with self-supply of ancillary services is very vague, (ii) potential unwarranted competitive advantage or cost discrepancies associated with self-supply of ancillary services are not unique to this procurement case and these options are available to all market participants in MISO, and (iii) FERC already found these provisions just and reasonable and approved them since they have been included in the MISO Tariff. Given the vagueness and weakness of the Companies' position on these issues and the lack of responsiveness to Mr. Ogur's rebuttal testimony, the Companies' recommendation against Staff's proposal should be rejected.

Fourth, given the lack of identification of any costs to the Companies or ratepayers and lack of evidence to suggest self-supply of ancillary services would give unwarranted competitive advantage to some suppliers, the claims presented by Mr. Blessing about the size, likeliness and duration of gains from implementing such an option should be rejected. Mr. Blessing merely states his opinion on these issues without support or any corroborating evidence in the record. Thus, it is clear that the option should be implemented for the simple reason that there are no costs associated with it to the Companies or ratepayers and there are potential benefits to the auction and ratepayers.

Staff Recommendation

Therefore, Staff recommends that the Commission accept Staff witness Ogur's proposal and order the Companies to modify the SFC language to include a provision to give the suppliers the option of self-supplying MISO Schedule 3 (regulation service), Schedule 5 (spinning reserve) and Schedule 6 (supplemental reserve) ancillary services.

f. Identification of Resources

In their initial filing, the Ameren Companies proposed that the suppliers be responsible for identifying their capacity resources to the Companies:

> The BGS-FP Supplier shall identify to the Companies, no later than December 1 of each year of the Term, or as otherwise necessary to permit the Companies to satisfy MISO or MAIN resource adequacy requirements, the resource or resources that it will use the following calendar year to

> provide Capacity to the Companies pursuant to the terms of his Agreement. The BGS-FP Supplier shall notify the Companies within 24 hours of any change in the resource or resources that it will use (or is using) to provide Capacity to the Companies pursuant to the terms of this Agreement.

(Resp. Ex. 3.1, p. 21, Section 2.1.b.(viii))

Staff witness Ogur recommended a change to the SFC in his direct testimony as follows:

> Placing an obligation on suppliers to provide to the Companies potentially commercially sensitive information, such as physical resources from which capacity will be provided, would have detrimental effects on participation in and competitiveness of the auction. To the extent information revelation is required by the suppliers for the Companies to meet their obligations to MISO or MAIN, it should be done in such a way that the Companies do not obtain such commercially sensitive information.

(ICC Staff Exhibit 4.0, p. 40, lines 871-877) Mr. Ogur provided four reasons for his recommendation.

First, obligating suppliers to submit the capacity resource information to the Ameren Companies may have adverse effects on auction participation. Some suppliers may consider such data as commercially sensitive, and thus may be hesitant to reveal the information to the Companies -- especially since the Companies' generation and marketing affiliates are competitors of the suppliers in the procurements auctions, bilateral energy and capacity markets, centralized day-ahead and real time RTO LMP markets and possibly many others. In order to avoid disclosure of such sensitive data, some suppliers may choose not to participate in the auction resulting in a less competitive auction, higher prices for ratepayers and possibly volume cutbacks by the auction monitor due to insufficient participation. (*Id.* pp. 28-29, lines 615-627)

Second, in order for the Ameren Companies to procure Network Integration Transmission Service ("NITS"), suppliers do <u>not</u> have to identify to them any resources because the pro-forma contracts will suffice for the Companies to procure NITS. (*Id.*, pp. 30-31, lines 656-670) Third, since resource adequacy obligations for the Companies' loads to the MISO will be met by the suppliers and these transactions take place via the Commercial Model, the suppliers do <u>not</u> have to reveal any information, which may be potentially commercially sensitive, to the Companies. (*Id.*, p. 33, lines 717-724)

Finally, the Companies may be able to meet their MAIN requirements without obtaining capacity resource information from the suppliers provided both MAIN and the Ameren Companies agree to such provisions. (Id., pp. 33-34, lines 727-747)

Ameren witness Blessing concluded in his rebuttal testimony that Mr. Ogur's recommendations are unnecessary and do not adequately address the Companies' legitimate concerns regarding resource adequacy. (Resp. Ex. 11.0 (Revised), p. 53, lines 1177-1180) Mr. Blessing made six arguments In support of his conclusion.

Mr. Blessing first argued that identification of specific capacity resources is not commercially sensitive information because the suppliers are not indicating that these same resources will be utilized to fulfill their energy obligations. (*Id.*, p. 49, lines 1092-1100)

Second, Ameren witness Blessing believes that the Ameren Companies' proposal is consistent with industry practice based on two purchased power agreements entered into by AmerenIP recently with affiliates of Dynegy, Exelon and Aquila. These suppliers apparently made no objections to being made to provide this data during negotiations. (*Id.*, p. 49, lines 1101-1105)

Third, Mr. Blessing is not aware of any potential supplier that objected to this portion of the Companies' proposal in the course of this proceeding. (*Id.*, p. 50, lines 1110-1114)

Fourth, although the Companies do not need capacity resource information from the suppliers for the procurement of NITS by utilizing SFCs as Designated Network Resources ("DNR"s), BGS suppliers will be precluded from having the ability to nominate and receive the specific financial transmission rights ("FTRs") that they will desire to hedge their congestion risk. It was not clear to Mr. Blessing what FTRs, if any, the suppliers would be entitled to should the Companies point to the SFCs as their capacity resources or DNR. (Id., p. 51, lines 1130-1144)

Fifth, the Companies, as the load serving entities, need to identify specific capacity resources in order to meet the resource adequacy obligations of the MAIN and they are not willing to turn this obligation over to a potentially large set of third parties. (Id., pp. 51-52, lines 1145-1156)

Finally, the capacity resource information of the suppliers is already available to the Companies or MISO market participants in general. The Companies can view the DNRs associated with their transmission service as the Transmission Customers. As Transmission Owners, they may also have access to portions of DNR data submitted in the NITS for planning, forecasting, and operational purposes. Existing DNR data, including MISO Generator Deliverability Test Results, is publicly available on the MISO website. Also available on the website is the MISO FTR allocation results as filed with the FERC, which include the identity of the asset owner, the source and the sink. (Id., p. 52, lines 1159-1173)

In rebuttal testimony, Staff witness Ogur continued to support his recommendation. (ICC Staff Exhibit 19.0. pp. 16-17) Mr. Ogur offered several arguments in support of his position. First, Ameren witness Dr. LaCasse considers capacity contract information as commercially sensitive. (*Id.*, pp. 19-20, line 402) In fact, in discussing a proposed modification to the competitive safeguards requiring auction bidders to disclose their wholesale purchase contracts for capacity and energy, Dr LaCasse states that “bidders will at best be reluctant to reveal their sources of supply” and “any contractual arrangements will be considered extremely sensitive business information.” (Resp. Ex. 12.0, p. 57, lines 1353-1357) She adds:

> Such disclosure requirements, if properly structured will have a chilling effect on participation as bidders will refuse to provide sensitive business information. Such disclosure requirements, if improperly structured, may well simply increase supplier costs as suppliers enter into more complicated contracts to avoid the need to disclose. The ultimate consequence on the auction of one or both of these effects of adding the disclosure requirements is to reduce competition or increase costs to suppliers, both of which can be expected to have a negative effect.

(Resp. Ex. 12.0, p. 57, lines 1361-1366)

Second, Ameren witness Blessing’s claim that the Ameren Companies’ proposal is consistent with industry practice is invalid. These negotiations are conducted between private corporations in a manner that is not open to the public; thus, no public record exists. Since the evidence Mr. Blessing is presenting cannot be verified, the assertions should be rejected. Further, “industry practice” is not determined by a few purchased power contracts or requests for power. Also, the nature of contract negotiations might require a party to deviate from its first preference on some issues in return for the counterparty doing the same on other issues. As a result, a party’s primary position cannot be determined by looking at the language of the final contract. Finally, a party may submit capacity resource information so that the purchasing company may evaluate the proposal. Since the examples Mr. Blessing mentions cannot be further analyzed, Staff cannot conclude that the Ameren Companies' proposal is acceptable simply by making such a comparison. Staff notes that industry practice may be contained in the SFCs proposed by ComEd in its procurement auction proceeding (Docket No. 05-0159) which does <u>not</u> require the suppliers to identify capacity resources to the buyer. (ICC Staff Exhibit 19.0. pp. 21-23, lines 455-494)

Third, Ameren witness Blessing admits that the BGS contracts are sufficient in MISO for the Ameren Companies to procure NITS, which is a process explained in Module B of the MISO Tariff. As a result, the Ameren Companies do not need to get capacity resource information from suppliers for NITS procurement purposes." (*Id.*, pp. 23-24, lines 498-522)

Fourth, Ameren witness Blessing's understanding that MISO limits its market participants to nominating and receiving FTRs based on the DNRs identified in the NITS procurement process, which assumes that MISO FTR allocations are based on DNRs designated under Module B of the MISO Tariff, is incorrect. MISO FTR allocations are in fact based on the DNRs designated under <u>Module E</u> (Resource Adequacy) of the MISO Tariff. The Companies have acknowledged that the phrase "NITS procurement process" is intended to encompass compliance with Module E of the MISO EMT. (*Id.*, p. 24, lines 523-537) "Thus, the suppliers do not need to submit capacity resource information to Ameren in order to be eligible to nominate FTRs. They can submit this information directly to MISO under Module E as market participants and this is sufficient to make them eligible to nominate and receive FTRs during the MISO FTR allocation period." (*Id.*, pp. 24-25, lines 537-552)

As explained above, the suppliers do not need to submit any capacity resource information to the Companies for the purpose of procuring NITS, as BGS contracts are sufficient for this purpose. Further, suppliers do not need to submit any capacity resource information to the Companies in order for the suppliers to be able to nominate and receive FTRs in MISO. Thus, Suppliers do <u>not</u> need to submit any capacity resource information to the Ameren Companies for any MISO-related purpose. (*Id.*, pp. 25-26, lines 553-665)

Fifth, Ameren witness Blessing's argument that the Companies take their obligations to the MAIN seriously and therefore are not willing to turn these obligations over to third parties is not valid. Turning the obligation over to the suppliers does not imply irresponsibility. Currently, the Companies meet their MAIN requirements by receiving the capacity resource information from the suppliers and then submitting that information to MAIN during MAIN's summer audit. Thus, instead of this two-step process, the Companies can simply allow the suppliers to submit required information directly and confidentially to MAIN on behalf of Ameren. (Id., pp. 26-27, lines 572-586) Further, ComEd is under exactly the same resource adequacy obligations to MAIN and yet is not requiring its suppliers to submit any capacity resource information to ComEd. (Id., p. 27, lines 587-589)

Even if we were to accept for argument's sake that capacity resource information is not commercially sensitive information, other commercially sensitive information might have to be submitted during the summer audit of MAIN, such as a supplier's contract for both energy and capacity from a generating unit, which Mr. Blessing acknowledges as commercially sensitive. (Id., p. 27, lines 590-602) Further, MAIN will likely be dissolved soon and be replaced by the ReliabilityFirst Corporation ("RFC"), which will function as a regional reliability coordinator encompassing a much larger region than MAIN currently does. As an expected RFC member, this may be a perfect opportunity for a large and influential Illinois utilities to make the case that the RFC should accommodate the realities of states or utilities that procure their power via BGS auctions. Finally, even if the requirement on the suppliers to submit capacity resource information to Ameren is retained, the SFC "December 1" deadline to submit such information should be changed. Since MAIN's annual audit is performed in the summer, there is no reason for the suppliers to identify capacity resources to the Companies as early as December 1 of each year. (*Id.*, pp. 27-28, lines 603-628)

Finally, none of the sources Ameren witness Blessing specified in his rebuttal testimony would allow the Companies to acquire the capacity resource information. Since no unit-specific DNR needs to be submitted under Module B for NITS procurement purposes, the Companies as the transmission customers do not need to see any units designated under their transmission service. Also Ameren witness Blessing is vague about the exact nature and extent of the DNR data the Companies will have access to that is submitted in the NITS process for planning, forecasting, and operational purposes. Moreover, the BGS suppliers do not have to submit any network resource information for the NITS process. Furthermore, even if the Companies may have access to some DNR information as the transmission owners, there is no need for the transmission owners to see the particular DNR designations of market participants.

Although, Staff witness Ogur agrees with Mr. Blessing that the MISO Generator Deliverability Test Results are publicly available, those test results do not make available the entities that designated the network resources. In addition, results of FTR allocations do not necessarily identify all of the DNRs of specific market participants. Even if the FTR allocation results allowed one to identify all of the DNRs of specific market participants, this is still not a sufficient reason to require the suppliers to submit capacity resource information to the Ameren Companies.

Ameren witness Blessing stated in his surrebuttal testimony that Mr. Ogur's recommended changes to the SFCs are not prudent given the current environment and market structure. (Resp. Ex. 18.0, p. 40) Mr. Blessing offered the following reasons for his conclusion:

a. Mr. Ogur's quote from Dr. LaCasse's testimony addresses another issue in another context and is not relevant in this context. The Ameren Companies clearly indicated what would be done with the capacity resource data. (*Id.*, 18.0, p. 38, lines 853-863)

b. In other purchased power agreement contexts suppliers were comfortable with providing capacity resource information to the Ameren Companies. (*Id.*, p. 39, lines 865-876)

c. ComEd is operating in a distinctly separate RTO which has its own rules and markets, therefore comparisons to ComEd contract provisions are not as relevant as Mr. Ogur suggests. (*Id.*, p. 39, lines 879-883)

Moreover, Mr. Blessing proposes conditions he believes the Commission should impose if the Commission were to accept Mr. Ogur's proposal:

> Should the ICC order the Ameren Companies to accept Mr. Ogur's suggested changes, they will obviously endeavor to comply, however it must be acknowledged that the provisions within the BGS contract cannot compel MISO, Mid-America Interconnected Network, Inc. ("MAIN"), or any other regional reliability organization ("RRO") to modify their business practices and administrative systems and that such business practices and system access may well conflict with the purpose of such change.

> Such an ICC order should, therefore, condition such an obligation on the Ameren Companies' ability to comply without violating standards of or obligations to MISO, MAIN, or any other RRO and without violating any applicable law or regulation.

(*Id.*, p. 40, lines 886-896)

In light of the foregoing, it is worthwhile to make some observations about the evidence in the record.

First, the Companies did not respond at all to Staff witness Ogur's claims in his rebuttal testimony that (i) Mr. Blessing is mistaken in his statement that capacity resource information the Companies are asking the suppliers to submit is already available to the Companies and other MISO market participants, and (ii) Mr. Blessing is mistaken in his statement that the suppliers cannot receive FTRs in the MISO FTR allocation process if they do not submit their capacity resources information to the Companies.

Second, there is simply no MISO-related reason for the suppliers to submit capacity resource information to the Companies. All the reasons Ameren witness Blessing gave in his rebuttal testimony were shown to be invalid by Mr. Ogur. Furthermore, Mr. Ogur claimed in his rebuttal testimony that since MAIN's annual resource adequacy audit is in the summer and since the only possible reason Ameren can need capacity resource information from the suppliers is to meet MAIN resource adequacy requirements, the suppliers should not be obligated to submit this information on December 1, but just in time for the MAIN summer audit. The Companies did not dispute this conclusion.

Third, the Companies did not respond Mr. Ogur's claim that the Companies will rely on the suppliers to meet their resource adequacy obligations, whether the information flows directly from the suppliers to MAIN or it flows through Ameren to MAIN The Companies also did not respond to Mr. Ogur's recommendation that they contact RFC, which is the successor organization to MAIN, to inquire about meeting resource adequacy obligations by information flowing from the suppliers directly to the RFC.

Staff Recommendation

Therefore, Staff recommends that the Commission accept Staff witness Ogur's recommendations and order the Companies to

i. Remove the references in the SFCs to the Companies' resource adequacy obligations to MISO in connection to acquiring capacity resource information from the suppliers;

ii. Remove from the SFCs the "December 1" date the Companies are obligating the suppliers to submit capacity resource information to Ameren on; and

iii. Contact the RFC with ICC Staff to propose to the RFC to satisfy the Ameren Companies' resource adequacy obligations to MAIN/RFC by direct information submittal from the suppliers to the RFC.

M. Other auction design issues

Staff reserves the right to respond in its reply brief to parties that address this matter in their initial briefs.

VI. PROCUREMENT PROCESSES ALTERNATIVES

In this section, Staff addresses the various alternative procurement processes that were suggested within the course of the proceeding. In keeping with the ALJ's desire for a uniform outline, these alternatives are addressed within the following categories:

A. Active portfolio management

B. Request for proposal

C. Affiliate contract

D. Other competitive procurement mechanisms

E. Other procurement process alternatives

However, there is significant overlap between active portfolio management, requests for proposal, affiliate contracts, other competitive procurement mechanisms, and other procurement process alternatives to the Ameren Companies' proposed vertical tranche SDCA auction. For example, active portfolio management (A) could entail using requests for proposal (B), affiliate contracts (C), other competitive procurement mechanisms (D) such as an auction for portions of the load (e.g., base load), and other procurement processes (E) such as directly buying or developing used or new generating assets or entering into bi-lateral negotiations with potential suppliers.

As Staff already noted in Section IV.A., the only such alternatives that have been presented in the record are vague or incomplete. Thus, the Staff recommends against their adoption by the Commission in this docket. Nevertheless, further discussion of these theoretical options is presented in the sub-sections, below. In the last sub-section (E. "Other procurement process alternatives"), Staff also addresses proposals to open a new docket to consider procurement options.

A. Active portfolio management

1. The case for active portfolio management

To one extent or the other, some of the AG and CUB witnesses argued in favor of so-called "active portfolio management." For example, in his direct testimony, AG witness Salgo stated,

> Given the scale of the proposed procurement, the Company should fully consider other approaches, including more ***active portfolio management***, utilization of the many other standard products available in the market, such as various standard blocks of power (such as base load 7x24 products) or unit contingent agreements and the possibility of negotiating prices and other contract terms with suppliers.

(AG Ex. 2.0, p. 11, lines 11-15, emphasis added)

Although waiting until his rebuttal testimony to really make the case for active portfolio management, CUB witness Steinhurst seemed to be the major proponent of the concept. For example, he testified:

> Because the relevant wholesale electricity markets are currently significantly flawed, because default service customers would face substantial and unwarranted risks in the proposed flash cut to auction procurement, and because the Companies should not be absolved of the duty to procure the best possible result for default service customers (especially in light of the open issues on past actions regarding divestiture), ***my primary recommendation continues to be that the Companies remain responsible for meeting those needs using a soundly designed and actively managed resource portfolio.***
>
> …
>
> There are many products that Ameren can combine into an ***actively managed portfolio*** design. … For example, in terms of power and energy, just a few of the products that should be evaluated to determine how their costs and risk profiles would affect default service rates include:
>
> • Standard wholesale electric power market forward contracts of various term lengths from a month to a number of years and a wide range of starting dates;

- Spot purchases;
- Bilateral negotiated contracts of varied terms, sizes or start dates;
- Unit-specific power contracts with owners of existing units;
- Non-unit-specific power contracts with owners of groups of existing units;
- Residual load following contracts;
- Options to buy (or sell) power at various prices at various times;
- At-cost, fixed price, turn-key or other types of arrangements for power from new or existing units at various locations.

(CUB Exhibit 4.0, p. 3, lines 55-62; pp. 17-18, lines 373-391, emphasis added)

Dr. Steinhurst also opined: that Ameren's procurement proposal fails to mitigate risks (*Id*., p. 19); that "obtaining a managed portfolio priced below the limited products on which the proposed auction would rely may well be possible through careful design and procurement" (*Id*., p. 21); that "actively managed procurement would allow flexibility in procurement decisions and negotiations" which would inure to the benefit of ratepayers (*Id*., p. 22); that "a soundly designed and actively managed portfolio for the benefit of default service customers can be an improvement in risk, price, or both compared to Ameren's proposed one-product, one-day-a-year auction." (*Id*., p. 23); that Ameren is capable of actively managing a portfolio for the Ameren Companies (*Id*., pp. 23-24); and that while "competition among the bidders will discipline *auction participants* to manage their portfolios, … Incorporation of prudence review and other ratemaking practices into the procurement process would give Ameren an incentive to better design and manage its portfolio" (*Id*., pp. 24-25).

2. The relationship between active portfolio management and prudence

Under cross examination, Dr. Steinhurst backed away from his insistence that "my primary recommendation continues to be that the Companies remain responsible for meeting those needs using a soundly designed and ***actively managed*** resource portfolio." (CUB Ex. 4.0, p. 3, emphasis added) Consider this exchange between counsel for Ameren and Dr. Steinhurst and Counsel for ComEd and Dr. Steinhurst:

Counsel for Ameren

Q. And as I understand your testimony, your are saying, one, reject this proposal and open a broader procurement docket, is that right?

A. That's one alternative recommendation, yes.

Q. That's your primary alternative, isn't it?

A. Yes.

Q. And you say then, secondarily, if you don't do that, you should require Ameren to use an actively managed portfolio design, is that correct?

A. No.

(Common Tr., p. 471)

Counsel for ComEd

Q. Let me begin by trying to understand exactly what it is that you are asking the Commission to do in this docket. As I understand it, your principal recommendation for Commonwealth Edison mirrors the recommendation you made with respect to Ameren that you explained to Mr. Flynn a few minutes ago, is that correct?

A. Yes.

(Common Tr., p. 478)

Q. Do you firmly recommend today that the ICC require ComEd to engage in active portfolio management under a regulated plan process?

> A. Not exactly. I tried to explain in my testimony why that would be a better approach than the company's proposal. But my primary recommendation is to leave the responsibility for the decisions about how to procure default service power with respective utilities.

(Common Tr., p. 479) As indicated by Dr. Steinhurst's response on page 478 of the transcript, Dr. Steinhurst's position is the same towards Ameren.

Dr. Steinhurst also admitted that there is nothing inherently unjust or unreasonable about private companies selling and utilities buying wholesale power at market rates (Common Tr., p. 480-482). In fact, he clarified that he is "not opposed in principle to auctions as part of a procurement methodology and auction-based procurements can have benefits." (*Id*., p. 487) Furthermore, he agreed that if a utility uses an auction-based procurement process which the Commission determines is "just and reasonable and prudent" and it uses the power that it acquires pursuant to that process to serve its retail customers, that the utility should be able to recover the resulting costs in its rates (*Id*., p. 489); and that he "would not recommend that anything preclude the judicious use of competitive procurement" by utilities meeting their default service obligations. (*Id*., p. 492)

In effect, Dr. Steinhurst recommends that the Commission let the Ameren Companies go about procuring power in any manner as the companies see fit, and afterwards the Commission can let them know how much of the resulting procurement costs are recoverable, using "traditional regulatory standards of justness and reasonableness, which entail a prudence review of the companies' decisions." (CUB Ex. 2.0, p. 8) He seems to prefer active portfolio management because that would give the Commission the maximum latitude to determine which of the many portfolio management decisions turned out to be imprudent. Giving the Ameren Companies the additional discretion to choose between "active portfolio management" and other alternatives (perhaps even a vertical tranche auction, as implied by his testimony during cross examination) provides even ***more*** ways of finding the companies imprudent.

In Staffs view, if the Commission were to find (e.g., in this docket) that the proposed auction process is a just and reasonable mechanism to use to secure power and energy, it strains the bounds of fairness to subject the Ameren Companies to after-the-fact prudence reviews, except for those aspects of the process where the companies retain discretion. Staff's position, in this docket, has been to remove as much discretion as possible from Ameren Corporation and the Ameren Companies and place it in the hands of a transparent competitive process that would be pre-approved by the Commission.

3. The case against active portfolio management

In this case, active portfolio management raises several concerns for Staff, which are discussed in this sub-section.

First, active portfolio management, by definition, places significant discretion in the hands of the utility company with regard to purchasing power and energy. As already noted, Ameren Corporation owns large power generating and marketing affiliates. Their existence supplies the Ameren Companies with a conflict of interest. Thus, in what would amount to a beauty contest between one complex procurement plan and another complex procurement plan (with a multitude of criteria for selection), it would probably be as difficult for Ameren to avoid playing favorites as it would for the Commission to determine if that were happening. This type of problem is avoided to a tremendous extent through the vertical tranche auction approach, where all the criteria for selection have been worked out in advance and presented to the Commission for its approval, and the focus of the auction is on only one completely objective criteria: <u>price</u>. As Staff witness Zuraski explained:

> In terms of dealing with market power and affiliate abuse concerns, the transparency of the vertical tranche auction is its central strength. This transparency is provided by the uniformity of the auctioned vertical tranche full requirement product as well as the bidding mechanism of the auction. … Suppliers are, in the end, evaluated solely on the price upon which they can supply a pre-defined product.

(excerpt from page 12 of "The Post-2006 Initiative: Final Staff Report to the Commission," released in November 2004, quoted in ICC Staff Exhibit 12.0, p. 5)

Second, despite the grandiose claims made by Mr. Salgo and Dr. Steinhurst concerning the efficacy of active portfolio management, there is no hard evidence to support these claims. Indeed, to the contrary, the evidence seems to suggest that state-supervised active portfolio management produces less-efficient outcomes. For instance, Mr. Steinhurst indicated during cross examination that he had been the Director for Regulated Utility Planning at the Vermont Department of Public Service and was in charge of Vermont's energy planning (which Staff assumes is akin to active portfolio management) for 14 years before leaving in 2003. (Common Tr., pp. 466-467) When asked if at the time he left the Department, Vermont's retail electric rates were over ***"40 percent higher than the national average,"*** he admitted, "I don't remember the precise number, but they were well above the national average at the time." (Common Tr., pp. 469-470)

Third, recall Dr. Steinhurst's assertions about the enormous flexibility of active portfolio management:

> There are many products that Ameren can combine into an ***actively managed portfolio*** design. … For example, in terms of power and energy, just a few of the products that should be evaluated to determine how their costs and risk profiles would affect default service rates include:
>
> - Standard wholesale electric power market forward contracts of various term lengths from a month to a number of years and a wide range of starting dates;
> - Spot purchases;
> - Bilateral negotiated contracts of varied terms, sizes or start dates;
> - Unit-specific power contracts with owners of existing units;
> - Non-unit-specific power contracts with owners of groups of existing units;
> - Residual load following contracts;
> - Options to buy (or sell) power at various prices at various times;
> - At-cost, fixed price, turn-key or other types of arrangements for power from new or existing units at various locations.

(CUB Exhibit 4.0, pp. 17-18, lines 373-391, emphasis added)

Well, this is not just a list of what resources are available to Ameren; it is also a list of resources available to <u>all</u> suppliers that would bid into the Ameren/ComEd vertical tranche auction. Hence, it is not a utility advantage of active portfolio management. Indeed, getting back to the relative value of utility regulation versus reliance on market forces,

> Neither Mr. Salgo nor Dr. Steinhurst recognizes the benefits of competition for the portfolio management service. … The point that Mr. Salgo misses is that when the portfolio management service is in the hands of the competitive market, as it is in the Auction Process proposed by Ameren, the competitive suppliers are the ones who will decide how efficient it is to leave some of the position open. The competitive suppliers will factor any such advantages directly into their bids. Customers will get the benefit of such cost minimizing strategies, and they will get this benefit at a fixed price.

(Resp. Ex. 12.0, pp. 16-17, lines 394-408)

Similarly, with respect to suggestions that active portfolio management would better mitigate risks, Dr. LaCasse explained that

> …the full requirements product places price-risk and responsibility for portfolio management in the hands of competitive entities that are best suited to take, manage and price these risks. This assignment of risks to the entities best positioned to manage them assures that the portfolio management service will be performed as efficiently as possible and that customers will benefit.

(*Id.*, p. 21, lines 504-509)

In summary, Staff does not believe that there is sufficient evidence in the record to reject the proposed SCDA approach for what some witnesses have referred to as "active portfolio management." Indeed, even those witnesses who seem to be most inclined toward active portfolio management have not gone so far as to actually recommend that the Commission order the utilities to utilize the approach. Rather, they prefer to let the Ameren Companies and ComEd make that decision, themselves, at their own peril. In contrast, there are several advantages of the SDCA (over active portfolio management) that have been firmly established in the record. Thus, for all the above reasons, Staff respectfully recommends that the Commission reject active portfolio management at this time.

B. Request for proposal

Requests for proposals, auctions, bilateral negotiations, and purchases from the centralized PJM markets are all alternative ways of obtaining contracts for power from markets. Hence, using a request for proposal ("RFP") does not imply that the utility can avoid going to markets. At one extreme, RFPs could be used to solicit bids for new generating equipment--either turn-key operations or components. Several different RFPs could be used to solicit bids for base load, intermediate load, and peaking load (consistent with the "active portfolio management" approach discussed in the previous sub-section). At the other extreme, RFPs could be used to solicit bids for vertical tranches (i.e., percent of full-requirements load), as in Ameren's proposal. In other words, a request for proposal is merely an alternative to using an auction process for soliciting bids from potential suppliers.

The relative disadvantages to requests for proposal versus an auction process have already been discussed in Section V.A. and V.E. Briefly, though, as Staff witness Zuraski explained:

> Relative to requests for proposal … an auction for a uniform product increases the comparability of offers. … Since all potential suppliers are ultimately judged on the same observable criterion, this minimizes the potential for utilities to provide favorable treatment to their affiliates, and reduces the burden of regulatory oversight. The bidding mechanism also provides a means for bidders to have their bids considered objectively, fairly, and simultaneously, further adding to the transparency to the process.

(excerpt from page 12 of "The Post-2006 Initiative: Final Staff Report to the Commission," released in November 2004, quoted in ICC Staff Exhibit 12.0, p. 5)

Ameren witness LaCasse presented a more complete list of the *pros and cons* of auctions versus requests for proposal:

> As I stated earlier, open auctions are likely to provide important economic benefits in contexts such as BGS procurement for the Illinois utilities and open auctions are likely to have significant advantages over the use of a sealed bid ("RFP") process.
>
> In general in an open auction, bidders are provided with market information round by round, and bidders can revise their bids and re-adjust their bidding strategy on that basis. This is in contrast to an RFP, where bidders must make all decisions regarding their bids and their strategies before submitting their proposal, and where bids are generally

> evaluated without bidders having the flexibility to revise their offers in light of new market information.
>
> …
>
> Bidders face less uncertainty than in an RFP process in which they would have to bid without the benefit of this valuable information. The flexibility to re-adjust bids takes away some of the guess work in bidding that is present in an RFP. When bidders face less uncertainty and guesswork, bidders have more confidence and tend to bid more aggressively. Bidders tend to be more willing to supply at lower prices. This aggressive bidding results in prices that are more competitive and better for consumers. This is an important economic benefit of open auctions in this context.

(Resp. Ex. 6.0, pp. 16-17, lines 364-373; pp. 17-18, lines 389-396)

Finally, as far as Staff can tell, no witness has actually proposed that Ameren utilize RFPs as a means to solicit bids for power in the post 2006 era. Hence, Staff respectfully recommends that the Commission reject substituting one or more RFPs for the proposed auction process, at this time.

C. Affiliate contract

As previously noted, the Ameren Companies have electric generating and marketing affiliates. Indeed, they are currently receiving its power for resale to its retail customers via affiliate contracts. The auction also holds out the possibility that such affiliates could win some (but not 100%) of the contracts to continue supplying this load after 2006. The suggestion has also been made by CUB witness Steinhurst, albeit obliquely, that a continuation of contracts with affiliates holds the key to the Ameren Companies acquiring power at more attractive "cost-based" rates rather than "market-based" prices:

> The Ameren Companies have "publicly stated that they presently anticipate average rate increases in the range of 10-20% for Illinois electric operations as a whole." Ameren Resp. to CUB DR 1.32. This is

> an increase in the bundled rate due only to the power supply component. (CUB Exhibit 2.0, p. 13)
>
> …
>
> In my prefiled testimony in a related Commonwealth Edison proceeding before the Commission, I estimated that a shift to pricing all power at market clearing prices stands to cost Commonwealth Edison ratepayers as much as $1 Billion per year relative to cost-based procurement. *[footnote omitted]* A copy of that study is attached as CUB Exhibit 2.2. While I have not performed a similar study for Ameren, I believe that a clearing price auction, where one pays the price of the most expensive offer for all power used, is likely to impose costs on BGS customer load that are substantially greater that those that would have flowed from traditional cost-based ratemaking.

(CUB Ex. 2.0, p. 13, lines 282-285; p. 16, lines 353-361) Although it is unclear whether it is supposed to follow from the above analysis, Dr. Steinhurst recommended that:

> The Commission could reject the competitive procurement and require Ameren to procure least cost power under traditional cost recovery standards. Such procurement would be subject to traditional ratemaking standards.

(*Id.*, p. 18, lines 393-395)

However, as Mr. Zuraski explained,

> Although some may find it distressing that rates could rise by such degrees, it is unclear how the Commission can utilize Dr. Steinhurst's assessment in this case. The fact of the matter is that, pursuant to the Customer Choice and Rate Relief Law of 1997, the Company was allowed to divest itself of its generating assets. Thus, unless the generating assets are bought back by the Company, the historical cost of those plants and the cost of operating them cannot directly form the basis for a reassessment of the Company's rates following the rate freeze. These plants are now a part of "market" supply. From the Company's perspective, the cost of producing power and energy from these plants is not and may never again be determined by an accounting of the cost of building and operating the plants. From the Company's current perspective, the cost of acquiring power and energy from these plants (or from any outside source) is determined by the market.
>
> Obviously, it would be desirable for ratepayers if wholesale suppliers could be convinced to provide power and energy to Illinois utilities at below-market prices. However, it is highly unlikely and

> unrealistic to assume that the Company can acquire power and energy at below-market prices, and Dr. Steinhurst provides no viable plan for making it happen.

(ICC Staff Exhibit 12.0, p. 7, lines 138-155)

In short, Dr. Steinhurst does not say how private companies such as the generating and power marketing subsidiaries of Ameren and ComEd—who are subject to FERC jurisdiction, who have market-based pricing authority, and who can sell into the PJM and MISO markets at market-based prices—could be compelled or convinced by this Commission to accept anything less than market-based prices.

Staff believes the Commission should accept Mr. Zuraski's conclusions, which are further supported in Section III. In particular, from the Ameren Companies' perspective, the purchase of FERC-jurisdictional wholesale power at market-based prices amounts to "cost-based" procurement. This Commission simply cannot prevent Ameren Generation (or any other such wholesale supplier) from being enriched by such sales, if its costs happen to be lower than prevailing market-based prices. Furthermore, assuming no accounting or rate design improprieties, such market-based purchases are fully consistent with the Ameren Utilities having "cost-based" rates. Based on the above discussion, Staff respectfully recommends that the Commission take no action to <u>direct</u> the Ameren Companies to acquire power from affiliates, but that the Commission recognize and accept that the proposed auction may result in Ameren affiliates supplying part of the Ameren Companies' full-requirement needs. In addition, Staff respectfully recommends against the Commission dictating to the Ameren Companies that they must negotiate or demand purchases from affiliates at anything other than FERC-approved prices, whether or not they are market-based.

D. Other competitive procurement mechanisms

See Section V.D. "Clearing Price: uniform versus pay-as-bid," where Staff discusses alternative auction proposals made by AG witness Reny.

Staff reserves the right to respond in its rebuttal brief to other parties who raise other competitive procurement mechanisms in their initial briefs.

E. Other procurement processes alternatives

1. Other procurement process alternatives presented in the record

Staff believes that it has addressed, within the sub-sections above, all the procurement alternatives presented in the record. However, Staff reserves the right to respond in its rebuttal brief to other parties who raise other procurement process alternatives in their initial briefs.

2. Proposals to open a new docket to consider procurement options

CUB witness Steinhurst recommended that the Commission: "[r]eject the Company's proposal," and "[o]pen a new docket to consider the full range of procurement options." (CUB Exhibit 2.0, p. 8) In contrast, AG witness Salgo, while recommending "that the Commission require Ameren to present a complete analysis of the rate impacts and risk levels for bundled customers associated with its proposed portfolio design and procurement method, compared with a variety of other portfolio design and procurement options." (AG Ex. 2.0, p. 23), further explained why it was "important to address these matters related to portfolio choice ***in this proceeding***." (AG Ex. 2.0, p.16, emphasis added) He also opined that:

> Consideration of various procurement options ***in this docket*** can ensure that alternatives to the full requirements auction are explored and evaluated now, before a crisis occurs.

(AG Ex. 2.0, p. 21, lines 16-18, emphasis added)

In reply to these calls for additional study, Ameren witness Nelson countered,

> The ICC should accept the Ameren Companies' proposal as offered and issue the orders necessary to permit implementation of the auction and the resulting retail rates. Importantly, there just is not time for the ICC to open a brand new docket and fully review in an adversarial context every possible procurement option. As described above, the Ameren Companies must procure power for January 1, 2007 deliveries. That means that between now and then, this proceeding must be fully adjudicated, the auction process (or procurement process resulting from this proceeding) must be fully developed, the auction must performed, and the winning suppliers must prepare to serve the Ameren Companies' customer load. Not only will a new docket not permit the full litigation of every possible alternative, it is simply not necessary. As described above, the Ameren Companies' proposal was developed as a direct result of the ICC's Post-2006 Initiative process and input from numerous interest groups.

(Resp. Ex. 10.0 Corrected, pp. 34-35, lines 798-810)

Staff witness Zuraski also expressed a lack of sympathy for holding more proceedings:

> I recommend that the Commission reject these proposals. In my opinion, these witnesses have not provided a sound or reasonable basis to "[r]eject the Companies' entire auction proposal" and "[o]pen a new docket to consider the full range of procurement options." First, there was nothing stopping parties that oppose the NJ model from presenting alternative models in the context of this proceeding. In this regard, it could not have been a surprise-- especially to anyone who was involved in the Commission's Post 2006 Initiative last summer--that the Company would be making a post 2006 procurement filing toward the beginning of 2005, and that it would likely propose something close to the NJ model. In any event, the clock has been and continues to be ticking, bringing us closer to the post 2006 era. The AG and CUB/CCSAO should have come to this proceeding prepared to present their alternatives to the NJ model rather

than with proposals to further delay the inevitable need to make decisions on viable procurement approaches.

(ICC Staff Exhibit 12.0, pp. 3-4, lines 47-60)

Legal aspects surrounding the issue of opening a new docket to consider the full range of procurement options are also discussed in Section III. Based on both the legal and the fact-based arguments, summarized above, Staff respectfully recommends that proposals to abandon the auction in order to hold additional proceedings should be rejected.

VII. TARIFF AND RATE DESIGN ISSUES

A. General tariff and rate design issues

The Commission should approve the tariff and rate design proposals presented by Staff in this proceeding. These proposals include: (1) a rate mitigation plan designed to shield rate classes from disproportionate increases in bundled electric bills; and (2) a definition of peak and off-peak periods that is consistent with current definitions for the Ameren Companies. These proposals are supported by strong arguments and compelling evidence. Furthermore, they have also been accepted by the Ameren Companies during the course of this proceeding.

Staff also recommends that the Commission reject a proposal presented by the Coalition of Energy Suppliers ("CES"). That proposal would implement for the Ameren Companies a rate migration factor such as ComEd proposed in its docket (Docket No. 05-0159). (CES Ex. 3.0, pp. 4-11, lines 85-216) The proposal presents a number of problems for the regulatory process.

B. Matters concerning Rider MV

1. Rider MV – Organization

a. The purpose of Rider MV and its Seven Sections

Rider MV is intended to (1) establish the methodology by which there is a translation of the wholesale market prices resulting from a competitive procurement process into seasonal and peak and off-peak values for use in calculating individual supply related charges in the Ameren Companies' retail tariffs; (2) describe the competitive procurement process for obtaining electric power and energy supply; and (3) account for the seasonal differentiation in payments made to suppliers. (Resp. Ex. 4.0, pp. 5-6)

Rider MV is divided into seven sections: Applicability (27.002), Purpose (27.002), Definitions (27.003), Competitive Procurement Auction Process (27.010), Limitations and Contingencies (27.029), Retail Customer Switching Rules (27.030) and Translation to Retail Charges (27.034). (Rider MV Original Sheet No. 27) According to the Ameren Companies, Rider MV has four major components. The major components are: "1) a detailed description of the auction process; 2) the contingency plans for procurement outside of the auction process; 3) the retail rate translation process; and 4) the market value price adjustment methodologies for reconciling the costs of power supply with the retail service revenues for supply service." (Resp. Ex. 4.0, p. 6) In addition, Rider MV also sets forth the retail customer switching rules (Rider MV, Original Sheet No. 27.030)

While all four of the major components of Rider MV are self-explanatory, Staff would note that with respect to the fourth major component, the reconciliation of costs of power supply with retail service revenue, Rider MV has two separate adjustment mechanisms. The first adjustment mechanism, Market Value Adjustment Factor

("MVAF"), is for supply obtained from the standard auction process. The second adjustment mechanism, Contingency Supply Factor ("CSF"), is for supply obtained outside of the normal auction process. (Id at 9) The MVAF tracks the monthly difference between retail customer revenue for supply services and the wholesale power supply costs obtained through the auction process. (Id at 9) The MVAF is intended to ensure that retail customers will pay no more and no less than the actual cost of power supply. (Id at 11) With respect to the CSF if supply is acquired outside of the auction process, the CSF computation would compare for a determination month the contingency power costs to the supply costs from prior auctions. The contingency supply costs are reduced by any default payments received. The cost difference is divided by forecasted customer usage for the respective billing month. The CSF is also adjusted with a balancing factor for any CSF inaccuracies from prior months. (Id at 11-12) The CSF is intended to recover only the incremental cost of contingency supply.

b. Rider MV needs a "Uniform" Index

Staff and the Ameren Companies were able to reach agreement that there was the need for a uniform index for Rider MV. Staff witness Harden testified in her direct testimony that the Ameren Companies should adopt an index for Rider MV that would be uniform with the index of ComEd's competitive procurement tariff. (ICC Staff Ex. 7.0, p. 3) Ms Harden's index was attached to her testimony as Schedule 7.1. (ICC Staff Ex. 7.0, Schedule 7.1) In their rebuttal testimony, the Ameren Companies indicated that Ms. Harden's standard index was acceptable, but did add that from time to time as circumstances warranted the Ameren Companies may seek to change the index. (Resp. Ex. 16.0, p. 9)

Staff recommends that the Commission adopt the uniform index for the Ameren Companies' Rider MV which was attached to Ms Harden's testimony as Schedule 7.1.

2. Rider MV – Definitions

a. Customer Supply Group definitions

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

b. Peak and Off-Peak Period definitions

The Commission should reject any proposal to revise the definitions of peak and off-peak periods for retail customers. Instead, the Commission should adopt Staff's proposed definitions that maintain consistency with the current definitions of peak and off-peak. Staff's proposal defines the peak period as 10 a.m. - 10 p.m., Monday through Friday (excluding holidays). (ICC Staff Exhibit 6.0, p. 33, lines 759-760)

The Ameren Companies proposed to change the definition of peak period to the hours of 6am – 10pm, Monday – Friday Central Prevailing Time (excluding holidays) in order to align with the definition that prevails in the Midwest Independent System Operator, Inc. ("MISO") markets of which the Ameren Companies are members. (Resp. Ex. 5.0, p. 10, lines 206-218) They justified their proposed change on the need to maintain a consistent approach between the retail and wholesale definitions. The Companies also argued that this proposal promotes cost causation and equitable cost recovery principles by aligning the cost incurrence period and the pricing or cost recovery period. In addition, they contended that the proposal was competitively neutral with respect to the wholesale markets in which RESs participate. (ICC Staff Exhibit 6.0, pp. 29-30, lines 677-688)

These arguments fail to consider the most important factor to define the peak period, which is the relationship between customer demands and the wholesale cost of power. Simply put, the Peak periods should cover the part of the day when the demand for power is higher, more supply resources are needed and the cost of power is higher. Prices should increase during the peak to discourage demand and reduce the strain on resources needed to meet the elevated demand. (ICC Staff Exhibit 6.0, p. 30, lines 692-702)

From a cost standpoint, the Ameren Companies' proposal sets the Peak period too broadly, thereby overstating prices when demand is low and understating prices when demand is high. As a result, consumers will not have sufficient incentive to curb demands during the peak period, which may serve to drive up electricity costs over the long term. This is a significant price to pay for the Ameren Companies' desire to align the retail and MISO wholesale peak and off-peak periods. (ICC Staff Exhibit 6.0, pp. 30-31, lines 704-709)

Furthermore, the Companies have not been consistent in their efforts to align retail and wholesale market prices. Their proposed translation prism does not directly pass the prices paid to suppliers along to ratepayers. Instead, it creates differences between the prices the Ameren Companies pay in the wholesale market and the prices consumers pay in the retail market. In addition, while auction prices are not differentiated by time of day, the Ameren Companies will recover power costs through

Peak and Off-Peak rates for larger customers. (ICC Staff Exhibit 6.0, pp. 31-32, lines 726-733)

The Staff proposal seeks to maintain consistency with the existing definitions of peak and off-peak periods and offers significant advantages over the Company proposal. First, it removes from the Peak period the hours of 6 a.m.-10 a.m. when demands on the system and the need for supply resources are low. Second, the continuity with the current Peak period offers benefits to customers who are on time-of-day rates and have aligned their consumption behavior to take advantage of the current definitions of Peak and Off-Peak hours. If the Peak period was more broadly defined, these customers would have to change their consumption behavior once again to save money. In addition, precedence exists for divergence between the retail and wholesale peak periods. New Jersey utilities do not consistently adhere to the 6 a.m.-10 p.m. (Central) Peak period prevailing in the PJM wholesale market to devise Peak periods for their retail customers. (ICC Staff Exhibit 6.0, pp. 33-34, lines 760-777)

In rebuttal, the Companies agreed to drop their proposed changes to the definitions of Peak and Off-Peak periods and accepted the Staff proposal. (Resp. Ex. 15.0, p. 13, lines 269-271) This removed any expressed opposition to the Staff proposed definitions of peak and off-peak periods. The Company's acceptance, combined with the clear evidence, strongly support the Staff-proposed definitions for peak and off-peak periods. Thus, Staff recommends that the Commission adopt its proposed definitions of Peak and Off-Peak periods.

3. Rider MV – Specification of Competitive Procurement Process

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

4. Rider MV – Retail customer switching rules

a. Enrollment window

The Ameren Companies proposed that customers eligible for the BGS-L product would be subject to an "enrollment window" in which customers would have 30 days after the conclusion of the auction to determine whether to take BGS-L service for the length of the supply period (initially, January 2007 to May 2008). (Resp. Ex. 3.0. p. 38, lines 819-823) Except for new customers, any customer that does not sign up during the enrollment period would be ineligible to take BGS-L service until the beginning of the next supply period. The selection of the 30-day enrollment period was not based on any empirical analysis. (ICC Staff Exhibit 5.0, p. 5, lines 113-115)

All parties recognize that it would be appropriate to impose a switching restriction in the form of an enrollment period on BGS-L customers, since BGS-L customers have demonstrated a significant propensity to switch from the Companies' service to service from a RES. These parties recognize that there is a trade-off between accommodating retail competition and the possibility that bidders may add a risk premium to their bids as a result of the uncertainty in estimating the size of the BGS-L load they would have to serve and the possibility of adverse market price movements during the enrollment period.

Staff witness Schlaf summarized the tradeoff issue as follows:

> …. the additional time afforded customers to shop also provides more time for wholesale market prices to evolve. Thus, it presents greater potential for RESs to make cost-saving offers to retail customers. Bidders in the [BGS] service auction would of course recognize that movement away from their service would coincide with a fall in market prices. To compensate for this risk, they would be less willing to offer supply in the auction without a higher risk premium….Thus, the beneficial effects of a longer enrollment window would not come without imposing a cost on the customers that do not want to switch away from bundled service.

(ICC Staff Exhibit 13.0., p. 3, lines 63-73)

The Ameren Companies' proposal was supported by Staff and the IIEC. Staff witness Schlaf stated that in the absence of empirical analysis showing the effect of an enrollment period of a given length on supplier bids, it would be difficult to assess whether customers should have 30 days, or some longer period, to decide whether they wish to take the BGS-L service. Dr. Schlaf noted that RESs and customers cannot make their deals instantaneously, and thus need some amount of time to arrange their contracts. On the other hand, the longer the enrollment period, the higher the risk premium that suppliers would add to their bids. (ICC Staff Exhibit 5.0, p. 6, lines 124-127) Thus, Staff supported a 30-day enrollment period. The IIEC, which represents large customers, also expressed support for the 30-day enrollment period, and stated that 30 days represents a reasonable compromise between allowing customers enough time to make supply decisions and minimizing supplier bids. (IIEC Exhibit 4.0 Corrected, p. 12, lines 252-255) CCG, the only potential bidder to comment on the issue, stated that even an enrollment period of 30 days would result in higher CCG generation charges as suppliers add a premium to their bids. (CCG Exhibit1.0, p. 3, lines 83-88)

The CES advocated a 75-day enrollment period. CES witness O'Connor noted that the 30 day enrollment period is especially problematic for many types of retail customers, such as school districts, governmental entities and hospitals, who employ lengthy committee processes to make decisions on a monthly basis. (CES Ex. 1.0, p. 31, lines 693-694) Additionally, companies that hire energy consultants and issue procurement requests might need more than 30 days to make their supply decisions. CES panel witnesses Domagalski and Spilky stated that 30 days is an insufficient amount of time to prepare bids for, and negotiate with, hundreds of prospective retail customers. (CES Ex. 3.0, p. 25, lines 526-529)

In response to claims that it would be impossible to verify whether a risk premium would exist if the enrollment period were increased from 30 days to 75 days, Dr. Schlaf presented an option pricing model in rebuttal to estimate the size of the risk premium that suppliers might be expected to add to their bids if the duration enrollment period were increased by a given number of days. The rationale for using this type of option pricing model is that customers hold an option for a certain number of days to buy the annual service product at a fixed strike price. Meanwhile, while customers are considering this option, offers from RESs presumably will be available in the market and their prices would follow the volatility of annual forward contracts. (ICC Staff Exhibit 13.0, p. 4, lines 82-90)

Dr. Schlaf found that suppliers might be expected to add about 3.2% of the forward price if the enrollment window were set at 30 days. For each additional 10 days that the size of the enrollment window is increased, bidders might be expected to add another 0.4% of the forward price to their bids. Thus, for an increase in the enrollment window from 30 days to 75 days, the model shows that suppliers might add about 1.8% of the forward price to their bids. (ICC Staff Exhibit 13.0, p. 4-5, lines 93-99) Dr. Schlaf considered the extra 1.8% a significant amount of additional cost. No other party presented empirical evidence on this issue.

Thus, following the submission of several rounds of testimony, there is a range of opinions on the duration of the enrollment window. While one customer group (IIEC) and a potential bidder (CCG), preferred a 30-day window, the RESs (CES) recommended 75 days. Staff recommended 30 days as the duration of the enrollment window.

Although all of the witnesses in this proceeding are advocating one of two proposed enrollment windows, the Commission is presented with more than two choices. That is, all of the reasons and rationales offered by the witnesses in support of a 30 or 75 day enrollment window can be considered in connection with the selection of an enrollment window between 30 and 75 days. The selection of an appropriate enrollment window necessarily involves striking a proper balance between the level of risk premium and impact on retail competition from a particular enrollment window. Thus, the Commission could select an enrollment window duration that is between 30 days and 75 days, with the understanding, of course, that enlarging the window would inevitably lead to somewhat higher costs for customers that remain on BGS-L service for the entire supply period.

Staff witness Schlaf agreed that such an alternative resolution should be possible. (Tr. at p. 1340, lines 3-5) He specifically agreed that enrollment windows of 45 and 40 days would be reasonable. (Tr. at p. 1340, line 2, and p. 1346, lines 13-20, respectively) Such enrollment periods would give RESs and BGS-L customers more time to negotiate deals, but at a cost (according to Dr. Schlaf's analysis, about an additional 0.4% to 0.5% of the forward price). Based on the above considerations, Staff respectfully submits that an enrollment window between 30 and 75 days would more appropriately balance the competing interests at stake than the end point positions advocated by the witnesses. Staff recommends that the Commission direct the Ameren Companies to modify its tariff so that BGS-L customers would have an enrollment window of 40 or 45-days. In Staff's view, this represents a significant increase in the time available to customers to make an election, while at the same time avoiding the imposition of a significantly increased risk premium. Staff, however, recommends against selection of an enrollment period longer than 45 days, given the level of added cost such larger enrollment windows would impose on BGS-L customers. Finally, Staff recommends that the Ameren Companies be required to study the issue of the appropriate duration of the enrollment period, and bring the results of its analysis to the attention of Staff and other parties prior to the next auction.

(1) Duration of window

With respect to duration of window, see Staff discussion in sub-section VII.B.4.a above. Staff reserves the right to respond in its rebuttal brief to other parties who raise other procurement process alternatives in their initial briefs.

(2) Opt in vs. opt out

With respect to opt in vs. opt out, see Staff discussion in sub-section VII.B.4.a above. Staff reserves the right to respond in its rebuttal brief to other parties who raise other procurement process alternatives in their initial briefs.

b. Other switching rule issues

The Ameren Companies' proposed switching rules are spelled out in proposed Rider MV (Original Sheets 27.032 and 27.033). In addition to BGS-L service, customers with a demand over 1 MW may elect to receive (1) hourly service, (2) RES service, and (3) PPO service (however, the price and terms and conditions for PPO service would be the same as the price, terms and conditions for BGS-L services).

Under the Companies' proposal, all customers that wish to take BGS-L service, except for new customers, must enroll for that service during the enrollment window. RES customers would be prohibited from moving to BGS-L service during the supply period, but could switch to hourly service. The Companies first proposed that bundled customers that have not made a supply selection would be switched to the hourly service, but later adopted Dr. Schlaf's recommendation that bundled customers that do not make a supply selection during the enrollment period could remain on supply service. (Resp. Ex. 15.0, p. 21, lines 445-448) New customers that start BGS-L service after the beginning of the supply must take BGS-L service for the remainder of the supply term. Staff does not oppose any of these proposals.

5. Rider MV – Limitations and Contingencies

The Ameren Companies initially proposed that all costs incurred through the contingency plan would be automatically passed through to customers. (ICC Staff Exhibit 5.0, pp. 14-15, lines 308-317) Dr. Schlaf, while agreeing that the Companies' proposed contingency plans were appropriate, recommended that the Commission retain the right to order refunds to customers should it find that the Companies' conduct contributed to the need to implement a contingency plan. (ICC Staff Exhibit 5.0, p. 18, lines 382-387) Dr. Schlaf noted that one circumstance in which it would be appropriate for the Commission to order refunds would occur if a supplier's failure to provide the supply called for under its contract resulted, at least in part, from the Companies' unjustified failure to pay the supplier in a timely manner. (ICC Staff Exhibit 5.0, p.17, lines 370-383) Another such circumstance was noted by Staff Witness Phipps, who explained that the Ameren Companies' management of their credit requirements might ultimately result in a supplier default. (ICC Staff Exhibit 15.0, p. 4, lines 74-79) In these, or any similar, situations, the amount that would be refunded to ratepayers would be the incremental cost of the replacement power (i.e., the replacement cost less the amount that would have been paid to the supplier).

In its rebuttal testimony, the Companies indicated that they would accept Dr. Schlaf's prudence proposal. (Resp. Ex. 10.0 Corrected, p. 28, lines 637-638) However, Ameren did not propose any new tariff language for this purpose. In rebuttal testimony, Dr. Schlaf offered tariff language to implement the proposal he offered in his direct testimony. (ICC Staff Exhibit 13.0, p. 9, lines 196-215) In their surrebuttal testimony, the Companies proposed a modification to Dr. Schlaf's proposed tariff language. Staff does not oppose this modification.

The revised tariff language provides that, should the Ameren Companies purchase electricity outside of an annual auction, they would first provide Staff a report concerning the circumstances of the purchases. The Commission could open an investigation to determine whether an act or omission of the Companies caused or contributed to the need for, or the amount charged to customers for, such purchases, whether such acts or omissions were imprudent, and, if so, whether refunds of any incremental costs (i.e., costs above what would have been paid under the SFCs) would be appropriate. Thus, Staff recommends that the Commission approve the proposed tariff language as modified by the Ameren Companies.

6. Rider MV – Translation to retail charges

The translation process allocates the winning auction prices paid to suppliers among the various rate classes receiving bundled electric service ("BES"). Under the proposed auction mechanism, suppliers will charge two prices for electricity supplied to the Ameren Companies: one price for the Summer months of June, July, August and September and a second price for the remaining non-Summer months. Those auction prices will not simply be passed along to ratepayers. Rather they will be recovered through separate charges to rate classes depending on how each class contributes to the cost of this power. The mechanism of breaking down supplier prices into component parts charged to rate classes has been dubbed the "translation prism". The specific rates that individual classes will pay for power are determined by three factors under the Ameren Companies proposed translation tariff: (1) when the classes consume electricity; (2) line losses the utility incurs in delivering electricity to them; and (3) generation capacity costs. (ICC Staff Exhibit 6.0, p. 3, lines 52-63)

The translation tariff does not present the actual power costs that customers will have to pay under Post-2006 rates. Instead, it contains a set of formulas and references to data inputs for those formulas that in combination would produce the power costs that bundled customers will have to pay. The reason formulas are necessary is that much of the essential data inputs will not become available until a future point in time. The missing data includes load data, forward prices and the winning auction power prices that will be known sometime in 2006. These auction power prices are multiplied by the translation tariff ratios to generate the power costs charged to the various customer classes. (ICC Staff Exhibit 6.0, p. 5, lines 101-115)

a. Customer Supply Group Migration Risk Factor

The Commission should reject the proposal by CES to implement a migration risk factor for the Ameren Companies customers. The CES proposal is flawed in both theory and practice. However, the Ameren Companies have failed to develop a migration risk factor proposal of its own. To fill the void, CES proposed a factor that was based upon the migration risk factor that ComEd proposed in its procurement proceeding (Docket No. 05-0159). CES not only relied on the ComEd proposal as a starting point for its Ameren proposal but also relied on the evidence presented in the ComEd docket. (ICC Staff Exhibit 14.0, p. 7, lines 157-161)

Staff has found the argument for the CES proposal to be incomplete. There are two key questions that need to be addressed concerning the migration risk factor: (1) is a migration risk factor appropriate for the Ameren prism?, and (2) if such a factor is appropriate, how should it be estimated? (ICC Staff Exhibit 14.0, p. 8, lines 166-169)

CES has failed to adequately answer these questions. For example, CES does not explain why a migration risk factor should be adopted for the Ameren Companies. Instead, CES takes the position that the discussion of the proposal in the ComEd docket is sufficient basis for it to be accepted in the Ameren case. (ICC Staff Exhibit 14.0, p. 8, lines 171-173) Instead of making a case for the migration risk factor, CES suggests that the burden lies with the Company to explain why it should not be implemented in the Ameren service territories. (CES Ex. 3.0, p. 5, lines 98-101)

Such a position presumes that migration risk is a well-established cost for suppliers and that the utility has the onus to demonstrate why it should not be included in the translation prism. However, CES provides no convincing evidence to demonstrate that it is a meaningful cost for suppliers that should be factored in the equation. (ICC Staff Exhibit 14.0, pp. 8-9, lines 184-188)

Further, CES argues that in this proceeding, the Commission should adopt the ComEd migration risk factor as revised by CES in Docket No. 05-0159. CES provides no arguments why the specific approach proposed by ComEd should be used for the Ameren Companies. Rather, it simply reprises its arguments from the ComEd docket for adopting its proposed revisions to ComEd's estimation methodology. (CES Ex. 3.0, pp. 6-9, lines 118-176)

The logic behind the CES argument is obviously flawed. The foundation for its proposed migration risk factor is the estimation formula proposed by ComEd. Nevertheless, CES presents no discussion or accompanying evidence in this docket as to why the ComEd approach should be used for the Ameren prism. The lack of support for the general formula renders moot the arguments by CES for revising ComEd's migration risk factor estimation formula. (ICC Staff Exhibit 14.0, pp. 9-10, lines 209-215)

CES further proposes that the Commission should use switching data for ComEd in calculating the migration risk factor for the Ameren Companies to address the lack of competition in the Companies' service territory. (CES Ex. 3.0, p. 11, lines 211-214) However, CES again fails to provide sufficient support for the proposal. Specifically, CES does not provide evidence that elimination of any obstacles to switching in Ameren's service territory would produce switching levels on a par with ComEd which is the assumption behind its proposal. This appears to be another case of the witnesses arbitrarily applying conclusions from the ComEd proceeding to the Ameren proceeding. This argument should be rejected along with the witnesses' entire proposal for imposing a migration risk factor on the Ameren prism. (ICC Staff Exhibit 14.0, p. 10, lines 225-230)

Thus, Staff recommends that the Commission reject the CES proposal implementing a migration risk factor for the Ameren Companies customers. CES has provided no relevant basis to support its proposal.

b. Market cost information – Market Energy Costs

In their filing, the Ameren Companies proposed that the market energy costs that would serve as the foundation for the translation prism should be based on forward energy prices. (Ill C.C. No. 35, Original Sheet No. 27.037; ICC Staff Exhibit 6.0, p. 25, lines 577-578) However, in direct testimony, Staff argued that the markets supporting these prices were thinly traded which called into question the value of forward prices. (ICC Staff Exhibit 6.0, pp. 25-27, lines 588-617) Staff further argued that Locational Marginal Prices ("LMPs") should be used instead to develop the prism. (ICC Staff Exhibit 6.0, p. 27, lines 620-621)

In rebuttal testimony, the Ameren Companies responded to Staff's proposal with further arguments as to why forward prices provide a more reasonable foundation than LMPs for market energy costs. First, they claim that forward prices have been accepted by the Commission for ratemaking in the development of PPO tariffs for both ComEd and AmerenIP. Second, the Ameren Companies contend that forward prices provide a better estimate of future prices than historical LMPs. Third, the Companies claim that the forward market is sufficiently liquid to serve as a foundation for market energy costs. Fourth, they state that LMPs present a problem because prices in non-summer months have exceeded summer prices over each of the past three years. (Resp. Ex. 15.0, pp. 9-13, lines 195-259)

Staff found the Companies' last argument concerning recent experience with LMPs to be determinative. Common sense indicates that power costs should be higher during the summer months than non-summer months, which has been the case in Illinois over the long term. Therefore, if forward prices reflect higher summer power costs than non-summer power costs, Staff accepts their use over LMPs for developing market energy costs despite misgivings about liquidity levels in the forward market. (ICC Staff Exhibit 14.0, p. 6, lines 127-133)

Thus, Staff recommends that the Commission use forward energy prices in developing the market energy costs that serve as the foundation for the translation prism.

7. Rider MV – Supply Procurement Adjustment

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

8. Rider MV – Market Value Adjustment Factor

a. Accounting reconciliations

See Section VII.B.9.a below

b. The SPA and Uncollectible Adjustment Should Not be Tracked Through the MVAF

The Commission should reject the proposal of Coalition of Energy Suppliers' ("CES") panel witnesses Domagalski and Spilky to track the Supply Procurement Adjustment ("SPA") and the uncollectible adjustment through the Market Value Adjustment Factor ("MVAF").

As proposed by the Ameren Companies, the Rider MV tariff is the rate mechanism by which the wholesale market price incurred by Ameren in the Auction is reflected in retail rates. (Resp. Ex. 4.0, p.7, lines 138-141) As part of Rider MV, the Ameren Companies have proposed two separate adjustment mechanisms -- one for supply obtained from the auction (MVAF) and another one for supply purchased outside the auction (Contingency Supply Factor). (*Id.*, p. 9, lines 185-187) The MVAF tracks "the monthly differences between retail customer revenue for supply services and the wholesale power supply costs for each of the auction categories under contract that are obtained through the standard auction process." (*Id.*, lines 187-191) The MVAF's purpose is to ensure equality between amounts paid to suppliers and amounts billed to retail customers. (AmerenCILCO, Ill. C. C. No. 18, Original Sheet No. 27.049;

AmerenCIPS, Ill. C. C. No. 16, Original Sheet No. 27.049; AmerenIP, Ill. C. C. No. 35, Original Sheet No. 27.049) CES panel witnesses Domagalski and Spilky recommend that the SPA and uncollectible adjustment be tracked through the MVAF to ensure that the Ameren Companies neither over recover nor under recover these costs. (CES Ex. 3.0, p. 19, lines 397-399; p. 27, lines 559-560; p. 28, lines 583-584) Ameren witness Mill indicated the Ameren Companies' acceptance of this recommendation with respect to the SPA. (Resp. Ex. No. 16.0, p. 4, lines 85-92)

Staff witness Struck disagreed with the CES' proposal. Mr. Struck explained that tracking the SPA and the uncollectible adjustment through the MVAF would not accomplish CES' stated goal of ensuring that the Ameren Companies neither over nor under recover these costs. In order to accomplish the kind of true-up intended by CES' proposal, one must reconcile costs incurred in a particular period with recoveries for that same period. Tracking the SPA and the uncollectible adjustment through the MVAF would not accomplish this kind of true-up. Instead, CES' proposal would reconcile recoveries for the Determination Month with the absolute dollar amounts from the test year in the last rate case. This would result in a mismatch of costs and recoveries from two different periods. These two different periods would likely reflect different levels of sales and different levels of costs. Thus, this kind of mismatch would not accomplish the true-up of costs and recoveries CES desires. (ICC Staff Exhibit 17.0, pp. 5-6, lines 96-118)

Mr. Struck also explained why such a true up is not necessary for the SPA and the uncollectible adjustment, both of which will be set in rate cases. When a rate is set in a rate case, that rate reflects a relationship between a given level of service and the cost to provide that level of service. So long as the relationship between costs and the level of service reflected in that rate remains within appropriate parameters, appropriate cost recovery occurs even when the level of service varies over different periods of time. (ICC Staff Exhibit 17.0, p. 6, lines 119-125)

In surrebuttal testimony, the Ameren Companies continued to disagree with Staff's position. (Resp. Ex. No. 23.0, pp. 3-5, lines 61-112) The Companies argue that without the adoption of the CES proposal to track the SPA through the MVAF, the Companies will always be in an over or under recovery position with respect to the SPA costs. (*Id.* 23.0, p. 4, lines 84-88) The Companies' argument is without merit. Once again, in order to achieve the kind of true up CES and the Ameren Companies seek, one must reconcile costs incurred in a particular period with recoveries for that same period. Instead, CES' proposal, which the Ameren Companies accept, reconciles recoveries for the Determination Month with the absolute dollar amounts from the test year in the last rate case. Such a reconciliation results in a mismatch of costs and recoveries from two different periods, which would likely reflect different levels of sales and different levels of costs. As a result, this kind of mismatch would not accomplish the true-up of costs and recoveries that is desired. (ICC Staff Exhibit 17.0, p. 6, lines 108-118)

The Ameren Companies' surrebuttal testimony merely highlights the fact that CES' proposal would not accomplish a legitimate true up. Instead, it would isolate a single cost element and force recovery for that cost element to an unchanging, predetermined dollar amount regardless of the level of service provided or amount of cost actually incurred. (Resp. Ex. No. 23.0, pp. 3-5, lines 68-99) Staff has explained why such a procedure is both incorrect and unnecessary. (ICC Staff Exhibit 17.0, pp. 5-6, lines 104-125)

In surrebuttal testimony. the Ameren Companies suggest that Staff is confused. Ameren witness Mill stated:

> It seems that the source of Mr. Struck's confusion may be his assumption that the MVAF would track SPA cost recovery against "actual" SPA costs as they develop prospectively, but that is not the case in my acceptance of the CES proposal. The Ameren Companies will not recover an annual amount of SPA that will exceed the level established in the prior rate case. This is so because we will monitor how much of the previously approved SPA amount is being recovered each month. The MVAF calculation will then be used to synchronize the actual cost recovery with the annual established SPA cost target.

(Resp. Ex. No. 23.0, p. 5, lines 92-99) Staff is not confused. Staff never assumed that "the MVAF would track SPA costs recovery against 'actual' SPA costs as they develop prospectively." As explained above, the problem with CES' proposal is that it would isolate a single cost element and force recovery for that cost element to an unchanging, predetermined dollar amount regardless of the level of service provided or amount of cost actually incurred. Mr. Mill's "clarification" merely highlights the reason Staff recommends the Commission reject CES' proposal. Staff witness Struck explained:

> CES' proposal would reconcile recoveries for the Determination Month <u>with the absolute dollar amounts from the test year in the last rate case</u>. This would result in a mismatch of costs and recoveries from two different periods. These two different periods would likely reflect different levels of sales and different levels of costs. Thus, this kind of mismatch would not accomplish the true-up of costs and recoveries CES desires.

(ICC Staff Exhibit 17.0, p. 6, lines 112-118 (emphasis added))

Staff strongly recommends that the Commission reject the CES' proposal for which the Company has agreed in part, to track the SPA and uncollectible adjustment through the MVAF.

c. Tariff Language for the Market Value Adjustment Factor ("MVAF") – Uncontested Issue

In direct testimony, Staff witness Selvaggio made a proposal regarding the tariff language for the MVAF proposed by the Ameren Companies (Proposed ILL. C. C. No. 16, Original Sheet No. 27.049). (ICC Staff Exhibit 8.0) The Company accepted Staff's recommendation to change the phrase used to represent costs in the Companies' proposed tariff setting forth the MVAF from "Payments that the Company makes to suppliers" to "Expenses the Company incurs". (Resp. Ex. 16.0, p. 5, lines 117-121)

Thus, Staff recommends that the Commission adopt its proposed tariff language with respect to the MVAF.

d. MVAF and Contingency Supply ("CSF") Formulas – Uncontested Issues

In direct testimony, Staff witness Selvaggio made various proposals regarding the formula to calculate the MVAF (Proposed ILL. C. C. No. 16, Original Sheet No. 27.050). (ICC Staff Exhibit 8.0) The Company accepted the following recommendations:

1. A definition for the term C in the Company's proposed MVAF formula was defined as set forth in Ms. Selvaggio's direct testimony (Resp. Ex. 16.0, pp. 5-6, lines 121- 125);
2. Language was added to provide for a Commission ordered reconciliation factor to refund or recover amounts ordered by the Commission (Resp. Ex. 16.0, pp. 6-7, lines 141-149). And
3. The Company provided a list of revenues, costs, and associated accounts that are to be included as components of the MVAF and the CSF for Commission approval (Resp. Ex. 16.0, pp. 9-10, lines 225-234).

Staff witness Selvaggio also recommended that the Remaining Balance Factor ("RB Factor") of the MVAF and CSF be modified to include a provision for interest. (ICC Staff Exhibit 8.0) However, Ameren witness Mill declined to modify the RB Factor for the MVAF. Mr. Mill expressed concerned that such a change would add to the complexity and cost of the administration of the MVAF and CSF and would require additional record keeping and accounting measure. Further, he contended there was no compelling reason for the inclusion of interest because (1) there will only be an average of 60 days between the time the MVAF or CSF is billed and the time when any resulting RB factor is reflected in a subsequent charge; (2) the most significant factor giving rise to the RB Factor is the difference between the forecasted and actual customer usage; and (3) the RB values will fluctuate due to variations of weather to normal. (Resp. Ex. 16.0, p. 6, lines 126-140) Staff agreed with Ameren and withdrew the recommendation to include interest in the RB Factor of the MVAF formula as the amount to be refunded/collected through the MVAF would likely not be material enough to warrant the provision of interest. (ICC Staff Exhibit 16.0, p. 2, lines 49-51)

However, Staff maintained that the RB Factor of the CSF formula should include a provision for interest or the definition of the RB Factor of the CSF formula should be modified. (ICC Staff Exhibit 16.0, pp. 3-5, lines 64-104) Ameren witness Mill agreed that "there should be an accrual of interest associated with the period the Ameren Companies hold the unamortized balance of default damages" (Resp. Ex. 23.0, p. 8, lines 178-180), but that the definition of the CPC Factor should be revised rather than the definition of the RB Factor. (Resp. Ex. 23.0, pp. 9-10, lines 193-207) Staff accepted the Companies' proposal. (TR 1131, lines 8-14))

Thus, Staff recommends that the Commission adopt the recommended changes as detailed above to the tariff language for MVAF and CSF.

9. Rider MV – Subsequent review / Contingencies

a. Ameren and Staff have reached agreement concerning Staff's Commission Oversight Recommendations

Staff witness Knepler had several concerns regarding the Commission's oversight role in connection with the proposed monthly "informational" filings and the true-up mechanism for the Ameren Companies' Rider MV. More specifically, Staff witness Knepler proposed four Commission oversight recommendations regarding monthly informational filing dates, public reconciliation hearings, internal audits and annual reports. His recommendations were as follows:

1. The MVAF and CSF mechanisms should be modified so that monthly filings are postmarked by the twentieth day of the filing month, any report filed after the twentieth but before the first day of the effective month would be accepted only to correct a previously filed timely report;

2. Rider MV should be modified to indicate that the Commission will initiate annual public hearings to reconcile the cost of electric power and energy purchased with cost recoveries;

3. Rider MV should be modified to require the Companies to file annual reports with the Commission; and

4. The Companies should perform annual internal audits of costs and recoveries recovered through Rider MV and submit such reports with the Manager of Accounting by April 1 for the previous calendar year.

(ICC Staff Exhibit 10.0, p. 10, lines 190-201)

On behalf of the Ameren Companies, Mr. Robert J. Mill accepted Staff's recommendations; however, he proposed that the three proposed annual reports (the reconciliation, the Rider MV report and the internal audit report) be combined into a single report and that the filing deadline of such a report be extended from April 1 to April 30. Mr. Mill further requested that should the annual report submitted to the Commission contain confidential information, that it be filed with the Chief Clerk's Office under such status. (Resp. Ex. 16.0, pp. 7-9, lines 154-207) In rebuttal testimony Staff witness Knepler found the proposed modifications discussed by Mr. Mill to be reasonable and therefore accepted the Ameren Companies' proposed modifications. (ICC Staff Exhibit 18.0, pp. 1-3, lines 12-42) Staff and the Ameren Companies are in agreement with respect to Staff's Commission oversight recommendations.

Thus, the Commission should adopt the Commission oversight recommendations made by Staff witness Knepler as modified by the Ameren Companies in Resp. Exhibit 16.0 (pp. 7-9, lines 154-207).

10. Alternative proposals re interruptible service

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

11. Other

a. Adjustments to Retail Supply Charges

Staff witness Struck proposed language changes to the introductory paragraph of Section 7. H., Adjustments to Retail Supply Charges of each respective Rider MV in order to clarify what is included in the adjustments to retail supply charges. (ICC Staff Exhibit 9.0, p. 3, lines 39-65) Ameren witness Mill indicated Ameren's acceptance of this proposed language. (Resp. Ex. 16.0, p. 9, lines 208-214) Thus, Staff recommends that the Commission adopt the Staff and Ameren agreed upon language.

C. Additional tariff and rate design issues

1. Staff's rate increase mitigation proposal

There are clear and compelling reasons to adopt the Staff proposal to prevent undue bill impacts arising from the auction process. Without the Staff plan, customer classes will be left to the vagaries of the auction process, the results of which will not be known for a number of months. When the dust settles from the auction, the potential exists for individual classes to receive inordinate increases relative to other classes. (ICC Staff. Exhibit 6.0, p. 18, lines 413-423)

The Staff proposal is essential to mitigate against any excessive increase in power costs that individual classes may receive. Further, it would apply only to the BGS auction whose customers have the fewest alternatives to bundled power. Staff's proposal would limit overall bill increases for these customers to the greater of the following: 20% or 150% of the overall BGS auction average. If the overall bill increase for customers within that auction is 13.33% or less, the maximum increase for any group of customers within the auction should be 20%. For an overall increase greater than 13.33%, the 150% of auction average limit would apply. (ICC Staff Exhibit 6.0, pp. 22-23, lines 514-521)

There are clear and compelling reasons for considering bill impacts in the ratemaking process for power costs. Utility bills can be a significant cost for ratepayers, both residential and non-residential alike. Significant increases in utility bills can have a disruptive effect on ratepayers' budgets. If the changes are sudden, ratepayers may not have sufficient time to make changes in their behaviors to absorb the higher cost. Thus, it may be necessary to limit those increases to give affected customers the opportunity to adjust to the new paradigm by introducing rate changes on a gradual basis. (ICC Staff Exhibit 6.0, p. 9, lines 191-197)

Bill impacts are a key regulatory issue in the current regulatory environment. They were a central component of the Restructuring Law, which enacted a rate freeze for non-residential customers and actual rate reductions of 5-20% for residential customers. By the time that new rates go into effect in 2007, this rate freeze and reduction will have been in effect for nine years. (ICC Staff Exhibit 6.0, pp. 16-17, lines 364-380)

The only factor considered in this rate freeze/reduction was bill impacts. No effort was made to determine the relationship of the frozen or reduced bundled rates to the underlying cost of service. Furthermore, when the rate freeze/reduction was revisited in 2003, there was no effort to align bundled electric rates with costs. Instead, the rate freeze and reduced rates were extended until the beginning of 2007. Thus, over the nine years following the enactment of the Restructuring Law, costs have deferred to bill impacts as a basis for setting bundled electric rates in Illinois. (ICC Staff Exhibit 6.0, p. 17, lines 382-389)

The Ameren Companies have indicated that customer impacts have been an important consideration for the ratemaking process, especially for the residential class. However, they initially argued that the Commission has the same latitude to approve inter-class subsidies for the generation component of electric service in the post-2006 era and stated that consideration of rate impacts on specific rate classes should have no role in this proceeding. (ICC Staff Exhibit 6.0, pp. 10-11, lines 223-252)

Nevertheless, the Company took an inconsistent position on this issue with respect to residential heating customers. The Company made an exception for these customers by proposing that residential heating customers receive a declining block rate during non-Summer months because such a structure "will help to mitigate concerns of customer rate impact, if any" (Resp. Ex. 5.0, p. 13, lines 267-274)

There are two reasons why bill impacts should play a central role in this case. One is the lack of information about Post 2006 rate levels. First, the Ameren Companies' proposed Rider MV contains formulas but no hard numbers. The actual power costs that customers will pay in the Post-2006 environment will depend on the input of future data into those formulas, which will not happen until the first auction is complete. Until the auction is conducted and the delivery services rate case is complete, potential bill impacts will not be known. This uncertainty also makes it difficult to develop proposals for mitigating bill impacts. Any remedy in this area must be prospective and designed to address potential scenarios that may or may not come to pass. (ICC Staff Exhibit 6.0, p. 18, lines 405-409)

Second, the Company is proposing a significant consolidation and realignment of bundled classes which can have a significant impact on bundled rates. The consolidation entails combining separate rates for customers for the three Ameren operating companies, AmerenIP, AmerenCILCO and AmerenCIPS, into one new set of rate classes. This consolidation and realignment can create adverse bill impacts independent of any change in power costs. These changes combined with the prospect of higher power and delivery costs provide good reason for concern about significant adverse bill impacts for customers. (ICC Staff Exhibit 6.0, pp. 17-18, lines 393-401)

The determination of an acceptable limit on bill impacts is necessarily a matter of judgment. There is no generally-accepted formula to apply to each situation. Instead, the particular circumstances of each proceeding must be examined individually to determine what the appropriate limits, if any, should be. The specific limit Staff proposes reflects the fact that bill impacts are both a relative and absolute issue. For example, if the imposition of Post-2006 rates increased total rates for all customers by 50%, the impacts would be severe, but no basis would exist to make any bill impact adjustments because the impact of the rate increase is equally shared. However, if the overall rate increase was 5% and one customer group faced an increase of 50%, then the increase for that customer class should be capped at a lower level. (ICC Staff Exhibit 6.0, p. 21, lines 476-491)

The Staff proposal seeks to reflect these two considerations. The maximum of 20% for overall auction increases of 13.33% or less recognizes that when the overall increase is lower, the relative increase for individual classes can be greater. Conversely, for overall increases greater than 13.33%, Staff's proposed limit of 150% of the average recognizes that when the increase is greater, it must be distributed more equally.

The adjustment process would take place after all components of the bundled ratemaking process are complete. That would include the current proceeding, the auction and the delivery service rate case. Then, the overall level of increase for customers would be used to determine which maximum, 20% or 150% of the CPP-B auction average, should apply. After that, current and Post-2006 bills for each proposed rate class must be calculated. If the increase for an individual rate class climbs above the applicable proposed maximum, then the power price for that class would be set at a level that brings the class back down to the designated maximum and the resulting revenue shortfall would be allocated on an equal percentage basis to all remaining classes. If that reallocation served to raise a class above the maximum, then the maximum would be applied to that class as well and the revenue shortfall would be reallocated again among classes not subject to the maximum. (ICC Staff Exhibit 6.0, p. 23, lines 525-537)

The Staff proposal is tied to the conduct of the auction. Under the translation tariff, power prices will be updated annually (after an initial 17-month period) to incorporate the results of auctions to replace expiring power contracts. Each time power prices are updated customers within the auction group would again be subject to the limit of the maximum of 20% or 150% of the average for the auction group. This would provide an opportunity to bring the power costs that customers pay further into line with the power costs they cause suppliers to incur, subject to these limits. Because future auctions will affect only a portion of overall power costs and not impact delivery services rates, there will be considerable latitude to bring the power costs that customers pay in line with the costs they cause to be incurred. (ICC Staff Exhibit 6.0, p. 24, lines 550-559)

Staff proposes that bill impacts be addressed solely within the context of the Rider-BGS auction. If total bills were capped for a group of customers, only customers within the BGS would be subject to an offsetting increase in power costs. So, for example, customers in the BGS-L auction would not be subject to an increase in power costs to offset a limit on bill increases for residential customers in the BGS auction. (ICC Staff Exhibit 6.0, p. 22, lines 505-510)

In fact, Staff's proposal does not extend in any way to the BGS-L auction for larger customers. That auction replaces the concept of a translation prism with a single, uniform price for power to be paid by all customers. There would be no room for any additional rate mitigation proposals under the concept of a single auction price for power. Furthermore, it would not make sense to have customers in one auction subsidize power costs paid by customers in another auction. That could create differences between the overall power costs paid by customers and power prices received by suppliers within an auction. That would add an unneeded level of complexity to the process. (ICC Staff Exhibit 6.0, pp. 20-21, lines 461-471)

The Companies responded to the Staff proposal in two ways. First, they indicated they were not opposed to Staff's rate mitigation proposal. However, the Ameren Companies went on to suggest two changes to the proposal. The first would postpone the bill impacts discussion until the Company's forthcoming delivery services cases. (Resp. Ex. 15.0, p. 4, lines 81-83)

The Companies noted that information is currently lacking concerning the actual bill impacts bundled customers will incur from the implementation of Post 2006 rates. Further, they contended that postponing the issue until the delivery services case will enable the Commission to address the issue with more information available because it will be determining the delivery services revenue requirement at the same time. (Resp. Ex. 15.0, pp. 4-5, lines 86-94)

In Staff's view it would be best to address this issue in the current docket for a number of reasons. This is an issue directly related to the translation prism; therefore, the reasons why the translation prism is addressed in advance of the delivery services case would apply to bill impacts issues as well.

Delaying the issue would prevent bidders in the upcoming auction from receiving a key piece of information concerning the recovery of power prices from customers. If the billing impacts issue is addressed in the delivery services case, the auction will be held before suppliers find out whether power costs would be subject to bill impacts constraints. This would undermine the goal of clarifying for suppliers how the translation would take place in advance of the auction. (ICC Staff Exhibit 14.0, pp. 3-4, lines 60-70)

Furthermore, postponing the issue to the delivery services docket would produce only one piece of additional information for Staff to craft a proposal on this issue. That information would be the Company's proposed delivery services revenue requirement. The auction prices and other inputs into the translation prism would remain unknown. (ICC Staff Exhibit 14.0, p. 4, lines 72-78)

Second, the Companies proposed that the Staff rate mitigation proposal be modified to permit Ameren to apply a single power cost for each rate class of all its operating companies. So, for example, residential customers from AmerenCILCO, AmerenCIPS and AmerenIP would be lumped together as a single group for determining bill impacts. This would enable Ameren to achieve its goal of "uniform BGS pricing throughout the Ameren Illinois footprint". (Resp. Ex. 15.0, p. 5, lines 99-105)

Staff opposes this proposal as well. It would undermine the objective which the bill impacts proposal seeks to achieve. A constraint that extends across the three

Ameren operating companies will not necessarily prevent an increase for customers within an individual operating company from exceeding the bill impacts maximum. Furthermore, it is not known today how much such an increase for customers from an individual operating company could exceed those maximums. This could leave a large group of customers facing an increase that far exceeds the levels deemed reasonable under Staff's bill impacts proposal. (ICC Staff Exhibit 14.0, p. 5, lines 95-105)

In sum, Staff recommends that the Commission adopt Staff's rate mitigation proposal. Further, the Commission should reject the Ameren Companies' revisions to the Staff proposal.

2. Uniform BGS pricing across Ameren Footprint, regardless of rate mitigation proposal

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

3. Rider D – Default Supply Service Availability Charge

The Ameren Companies proposed to impose the Default Supply Service Availability Charge ("DSSAC") charge on all RES customers eligible for Rider BGS-L and the customers in the customer group that choose real-time pricing service under Rider RTP-L. (Resp. Ex. 5.0, p. 18, lines 718-720; p. 34, lines 742-745) DSSAC charges paid by customers and collected by the Companies would be forwarded to successful bidders in the Rider BGS-L auction. The DSSAC is set at $0.00015/kWh (0.015 cents/kWh). (ICC Staff Exhibit 5.0, p. 10, lines 225-227) ComEd has not proposed a DSSAC-type charge in Docket No. 05-0159. (IIEC Exhibit 2.0, p. 16, lines 339-341)

The Ameren Companies are concerned that few, or possibly even zero, suppliers will bid in the BGS-LRTP auction, especially if they perceive that few customers will take Rider RTP-L To address this problem, the Companies have proposed to provide an incentive to bid, because winning bidders will collect revenue even if they do not serve any customers. (ICC Staff Exhibit 13.0, p. 6, lines 122-128)

The Ameren Companies' Rider D proposal was opposed by CES, IIEC and Staff. CES witness O'Connor described the proposed charge as "unduly discriminatory, unreasonable, unjust." (CES Ex. 1.0, p. 39, line 878) As Dr. O'Connor explained, the charge cannot be avoided by RES customers even if the customers have no interest in taking Rider RTP-L service:

> This pre-ordained price would be a noticeable add-on for customers who are not taking any utility supply service whatsoever, who may never take the hourly service, and who have not indicated an intention to take the service.

(*Id.*, p. 38, lines 852-855)

IIEC witness Dauphinais opined that charges for Rider RTP-L customers should be reflected in supplier bids, rather than being charged to RES customers:

> As such it is appropriate to reflect any price premium associated with the service in the rates for that service -- not as a non-bypassable charge applicable to customers not currently taking the service. Finally, the proposal does not allow bidders to compete to cover this risk. By this I mean the charge is fixed and not based on what price bidders are willing to accept to cover this risk. Therefore, bidders should simply be permitted to include any premium for this risk in their BGS-LRTP capacity bids.

(IIEC Exhibit 2 Corrected, p. 16, lines 345-351)

Staff witness Schlaf noted the Ameren Companies did not provided any evidence that winning bidders would reduce their bids by the amount of DSSAC, and instead, might simply pocket DSSAC revenue. (ICC Staff Exhibit 5.0, p. 12, lines 261-265) He noted that no supplier has stated in this proceeding that it will not bid unless it receives the DSSAC revenue. (ICC Staff Exhibit 13.0, pp. 6-7, lines 139-142) He also noted that RES customers would pay twice for capacity, once to their RES suppliers, and a second time in the form of the DSSAC. (ICC Staff Exhibit 5.0, pp. 12-13, lines 216-273)

Staff recognizes that the Ameren Companies must procure capacity for Rider RTP-L customers (should there be any). Staff also recognizes that the Companies' DSSAC proposal will very likely ensure that there will be at least one supplier willing to provide Rider RTP-L capacity, since suppliers might line up to bid for the chance to collect up to $1 million in DSSAC revenue, the amount that Staff estimated that RES customers would pay in DSSAC charges. (ICC Staff Exhibit 13.0, pp. 7-8, line 153) Staff believes, however, that it is unfair to charge customers for a service, (i.e., Rider RTP-L), that most customers do not want and have no intention of taking. Moreover, the Companies' solution would potentially have a negative effect (albeit a small one) on retail competition. (ICC Staff Exhibit 5.0, p. 13, lines 269-274) The Ameren Companies' should try a solution to any potential BGS-LRTP problem that does not impose a fee on non Rider RTP-L customers or detract from competition. Thus, Staff recommends that the Commission reject the Ameren Companies' proposed DSSAC charge.

4. “Default” BGS Rate for Large customers during Initial Open Enrollment Period, Company and Staff BGS-4, Coalition RTP

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

5. Inclusion of non-residential rate risk or migration premium as a factor in rate prism for larger BGS-FP customers

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

6. Treatment of Uncollectibles

Staff and the Ameren Companies agree that the Commission should determine both the methodology and value for the uncollectible adjustment in the Ameren Companies’ delivery services rate cases. (ICC Staff Exhibit 9.0, pp. 7-8, lines 147-162; Resp. Ex. No. 16.0, p. 3, lines 48-66) Staff and the Ameren Companies also agree that the Commission should use the modified Rider MV tariff language regarding the uncollectible adjustment set forth at lines 83-88 of ICC Staff Exhibit 17.0. (ICC Staff Exhibit 17.0, pp. 4-5, lines 80-95; Resp. Ex. No. 23.0, pp. 2-3, lines 46-48)

The Ameren Companies proposed to include in each respective Rider MV as an adjustment to its retail supply charges an uncollectible adjustment which would be determined based upon an average of the three (3) previous years of uncollectible expense as related to supply costs. (Resp. Exhibit 4.1-CILCO, Original Sheet No. 27.049; Resp. Exhibit 4.1-CIPS, Original Sheet No. 27.049; and Resp. Exhibit 4.1-IP, Original Sheet No. 27.049) Staff witness Struck noted that the Ameren Companies’ proposal would treat supply-related uncollectible cost differently than the rest of the non-commodity cost of procuring and administering power and energy supply. The proposal would adjust the amount of uncollectibles expense to be recovered annually, in between rate cases, without considering changes in the components of the other non-commodity costs, which would be changed only in rate cases. Staff witness Struck explained that, in order to evaluate the Ameren Companies' proposal, the Commission should evaluate the relationship between uncollectibles and the aggregate of the other non-commodity costs. Mr. Struck recommended the Commission determine the methodology and resulting value for the uncollectible adjustment in each of the Ameren Companies' subsequent rate cases. This would enable the Commission to evaluate the methodology and amount for the uncollectible adjustment while it is also evaluating the amounts for the other non-commodity costs of procuring and administering power and energy supply. Staff witness Struck proposed tariff language to reflect his recommendation that the Uncollectible Adjustment be determined in the Ameren Companies' rate cases. (ICC Staff Exhibit 9.0, pp. 4-9, lines 69-188)

Ameren witness Mill indicated the Ameren Companies' agreement that the Commission should determine both the methodology and value for the uncollectible adjustment in the Ameren Companies' delivery services rate cases. (Resp. Ex. 16.0, p. 3, ll. 48-66) However, Staff witness Struck noted that the revised tariffs provided by Ameren did not accurately reflect Ameren's acceptance of this position. Staff witness Struck recommended a further modification to the tariff language to correct this inconsistency. (ICC Staff Exhibit 17.0, pp. 4-5, lines 66-95) Ameren witness Mill noted the inconsistency in Ameren's tariff language and accepted Staff witness Struck's further modification to the tariff language. (Resp. Ex. No. 23.0, pp. 2-3, lines 35-48)

Staff recommends that the Commission adopt the following Staff and Ameren agreed upon language regarding the uncollectible adjustment:

> Uncollectible Adjustment
>
> This adjustment shall be established by the Commission in a delivery services rate case. The uncollectible adjustment will be based on the Company's uncollectible experience for Company-supplied power and energy. This adjustment will only apply to Customers taking power and energy from the Company.

(ICC Staff Exhibit 17.0, p. 5, lines 83-88)

7. Credit risk and other administrative costs

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

8. Integrated Distribution Company issues

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

VIII. CONCLUSIONS AND MIXED LEGAL/FACTUAL ISSUES

A. Legality of Rider MV

As explained in Section III.B above and Section VIII.C below, it is clearly within the Commission's authority to approve Riders BGS and MV. The question is whether based on the record the rates proposed under Rider MV are just and reasonable. A just and reasonable rate is a question of sound business judgment and is not the product of a legal formula. (Governor's Office of Consumer Services v. Illinois Commerce Com., 220 Ill. App. 3d 68, 580 N.E.2d 920, 162 Ill. Dec. 737 (Ill. App. Ct. 3d Dist. 1991)) As articulated by Staff throughout this brief, the Commission should find that the process for establishing rates under Riders BGS and MV is indeed based on sound business judgment and would result in just and reasonable rates. As explained throughout this brief, the election of an auction-based procurement process represents a prudent management decision as to the method to procure wholesale power and energy. The auction-based procurement process is fair, open and transparent, fosters competition, and is designed to result in the lowest possible prices for wholesale supply. The translation mechanism is designed to pass on to retail customers on a dollar for dollar basis (i.e., with no markup) the wholesale costs paid through the auction-derived wholesale supplier forward contracts. The analysis of the record evidence and applicable law set forth below demonstrates that the rates so derived should be found to be just and reasonable.

Sufficiency of the Competitive Market

Throughout this proceeding, there have been conflicting opinions on the competitiveness of the wholesale market for electricity and portions of the Illinois retail market for electricity. (Resp. Ex. 13.0, p. 3, lines 51-56; AG Ex. 1.0, p. 3, lines 17-22; CUB Exhibit 1.0, p. 3, Lines 45-52,) In Staff's view, the status of the competitiveness of the wholesale/retail electricity markets merely adds to the urgency and importance of approving viable and appropriate procurement methods for electric utilities to implement. As Staff witness Zuraski testified, "…even assuming, for the sake of argument, that the wholesale market is not competitive, that would not change the facts that (i) Ameren has an obligation to provide power and energy to most of its retail customers and (ii) the only conceivable place that Ameren will be able to acquire power and energy for delivery beginning in 2007 is the wholesale market.". (ICC Staff Exhibit 12.0, p. 8, lines 164-169)

Certain Intervenors, while raising concerns with the competitiveness of the wholesale market, have not provided a viable alternative for the Ameren Companies to procure the power and energy for its customers. Further, these concerns only increase the need to approve viable and appropriate procurement methods for electric utilities to implement. The Commission must ensure a viable procurement approach and, in Staff's view, at the present time the only viable approaches must necessarily rely on the wholesale market.

<u>Auction</u>

To meet its power and energy needs following the end of the transition period on January 1, 2007, the Companies propose to utilize a variant of a simultaneous "multiple round" auction, using a "descending clock" format (Resp. Ex. 2.0 Corrected, p. 19, Lines 402-407), which has also been called a "simultaneous descending clock auction." (ICC Staff Ex. 1.0, p. 6, lines 115-116)

Staff submits that the basic SDCA auction concept, as proposed by the Ameren Companies, is an appropriate competitive procurement method for securing power supply commitments for serving the Companies' retail customers and recommends that the Commission approve the basic SDCA approach. However, Staff recommended certain improvements to the SDCA, as detailed above in Section V. For instance, Staff witness Schlaf recommended a prudence review in certain circumstances when the Companies have to utilize its Contingency plan to procure power. The Ameren Companies and Staff were able to reach agreement on this issue. Staff believes the SDCA will deliver better results for Illinois ratepayers with its recommendations.

Tariff and rate design

Staff witnesses Lazare, Harden, Selvaggio and Knepler reviewed Rider MV as to its design. While Staff urges the Commission to accept all of its recommendations, the Companies have already agreed to significant improvements to Rider MV. For example, Staff witness Knepler proposed four Commission oversight recommendations regarding monthly informational filing dates, public reconciliation hearings, internal audits and annual reports. With slight modifications, the Ameren Companies accepted Mr. Knepler's recommendations. In addition, Staff witness Selvaggio made certain recommendations concerning tariff language with respect to the MVAF and CSF contained in Rider MV. The Ameren Companies and Staff were able to reach agreement on the respective language. Finally, Staff witness Harden and the Ameren Companies were also able to reach agreement concerning the uniform index for Rider MV.

Conclusion

Based on the record and for the reasons expressed above and throughout this brief, Staff believes that the Commission should find that Riders BGS and MV would result in just and reasonable rates.

B. Issues concerning compliance of auction process details with Illinois law

Staff believes that the auction process complies with Illinois law, and has no additional issues to raise at this time. Staff will address in its reply brief any additional issues concerning compliance of the auction process with Illinois law that may be discussed by other parties.

C. Other conclusions and mixed legal/factual issues

Staff witness Zuraski in his direct testimony stated that market prices as determined by the Ameren Companies' proposed auction or the MISO spot market as set forth in Rider MV would meet the description of market value as set forth in Section 16-112 of the Act. (ICC Staff Exhibit 3.0, p. 7) An analysis of Section 16-112 of the Act (220 ILCS 5/16-112) supports Mr. Zuraski's position. Section 16-112(a) provides that:

> ... market value …shall be determined in accordance with either (i) a tariff that has been filed by the electric utility with the Commission pursuant to Article IX of this Act and that provides for a determination of the market value for electric power and energy as a function of an exchange traded or other market traded index, options or futures contract or contracts applicable to the market in which the utility sells, and the customers in its service area buy, electric power and energy, or (ii) in the event no such tariff has been placed into effect for the electric utility, or in the event such tariff does not establish market values for each of the years specified in the neutral fact-finder process described in subsections (b) through (h) of this Section, a tariff incorporating the market values resulting from the

> neutral fact-finder process set forth in subsections (b) through (h) of this Section.

When interpreting a statute, one must first look to the plain language. *See e.g., Davis v. Toshiba*, 186 Ill. 2d 181, 184-85 (1999) The plain language of 16-112(a) provides that market value, if it is not the result of the neutral fact finder process (Section 16-112(a)(ii)), must meet three requirements. The first requirement is that the market value must be the function of one of three alternatives. Market value must be the function of either: (1) an index; or (2) an options or futures contracts; or (3) contracts. The second requirement is that the index, or options or futures contracts, or contracts must be a function of exchange trading or market trading.

The third and final requirement is that the index or the options or futures contract or the contracts must be applicable to the market in which the utility sells, and the customers in its service area buy, electric power and energy. The Commission in the past has interpreted the requirement that market value be determined "**as a function of**" one of the allowed indicators in a broad sense. The Commission in its order on reopening in ICC Docket Nos. 00-0259, 00-0395, and 00-0461 (Consolidated) rejected the IIEC's argument that the use of bids and offers was inconsistent with the 16-112. The Commission found the use of bids and offers would produce a market value that was determined as "'<u>a function of</u>' a market index." (ICC Docket Nos. 00-0259, 00-0395, and 00-0461 (Consolidated), Order on Reopening, at 162 (emphasis added))

Based upon the plain language of Section 16-112 and the Commission's prior orders concerning market value, the Ameren Companies' proposed market value determination method most certainly meets the three requirements. With respect to the first requirement, the Ameren Companies' proposed Rider MV relies on the SFCs which are the binding wholesale contracts the Ameren Companies will have with suppliers for the procurement of full requirements electric supply to serve their retail customers. (AmerenCILCO, Ill. C. C. No. 18, Original Sheet No. 27.007; AmerenCIPS, Ill. C. C. No. 16, Original Sheet No. 27.007; AmerenIP, Ill. C. C. No. 35, Original Sheet No. 27.007). Therefore, there can be no dispute that the SFCs relied upon in Rider MV are "contracts." With respect to the second requirement -- that the contract be a function of exchange trading or market trading, the Ameren Companies' witness Dr. Chantale LaCasse testified that "…the Auction Process can deliver reliable supply at competitive market prices." (Resp. Ex. 12.0, p. 2, lines 43-44) Accordingly, the contracts which result from the auction are a function of market trading. Staff witness Zuraski also testified that auction prices which result from a competitive procurement process would be the result of a market. (ICC Staff Exhibit 3.0, p. 6)

Finally, with respect to the third requirement -- that the contract be applicable to the market in which the utility sells and its customers buy power and energy, the SFCs are the contracts that will set forth the terms for the acquisition of electric power and energy by the Companies to be supplied to their customers. Accordingly, given the direct use of these contracts to provide power and energy to the Companies' retail customers, there can be no dispute that the SFC contracts are "applicable to the market in which the utility sells, and the customers in its service area buy, electric power and energy" (220 ILCS 5/16-112(a)(i)). With respect to contingency purchases, i.e., those purchases in the MISO-administered markets (AmerenCILCO Ill. C. C. No. 18, Original Sheet No. 27.029; AmerenCIPS Ill. C. C. No. 16, Original Sheet No. 27.029; AmerenIP Ill. C.C. No. 35, Original Sheet No. 27.029), those purchases undoubtedly would produce a market value which meets the three requirements of 16-112(a) since the MISO purchases would result in contracts which are a function of market trading and the power and energy purchases would be for the Ameren Companies' customers.

For all the foregoing reasons, Staff submits that Rider MV meets all of the applicable requirements for establishing market value via a tariff pursuant to Section 16-112.

IX. Other issues

A. Renewable energy and energy efficiency issues (not already addressed above)

CUB witness Steinhurst discussed the procurement of electricity from renewable resources and the procurement of energy efficiency resources. (CUB Exhibit 2.0, pp.32-39) Basically, he said that these resources could be procured through the Ameren Companies' proposed auction, but that he preferred that they be procured apart from the auction.

Staff witness Zuraski "strongly" opposed Dr. Steinhurst's less-favored recommendation to make renewable and energy efficiency purchases through the auction. If such resources are to be procured, he concurred that such procurement should be accomplished outside of the auction. (ICC Staff Exhibit 12.0, pp. 25-26) Noting that the Commission had recently issued a resolution adopting a policy of encouraging voluntary participation by electric public utilities in a plan to make greater use of renewable and energy efficiency resources, he testified that it was "totally unnecessary for the Commission to make any decisions about purchasing renewable and energy efficiency resources in this docket." (*Id.*, p. 26) However, he also opined that the Commission should reject any notion of making "earmarked purchases of renewable energy through the auction and purchases of energy efficiency resources through the auction." (*Id*.)

In arguing against making special earmarked purchases of renewable energy through the auction, Mr. Zuraski testified that

> There are no artificial barriers preventing renewable power developers from participating in the auction. The only barriers that may exist are due to the lack of expected profitability of renewable power at market prices. If renewable power production is generally more expensive than conventional power production, I would not be surprised if suppliers' intent on relying on renewable power would be reluctant to compete head-to-head in the auction. However, this should not be remedied with special treatment or set-asides for renewable power within the auction. The end result of such special treatment can only be price increases, especially in the initial post-2006 period, when ratepayers already may be subject to significant price increases due to the end of the price freeze currently in effect for bundled customers.

(*Id.*, lines 546-556)

In arguing against making special purchases of energy efficiency through the auction, he testified that

> The concept of ***energy efficiency resources*** is fundamentally different than the concept of ***a supply of energy that is meeting vertical tranches of load***. First, there is the problem of measuring reductions in load, which is intrinsically speculative and imprecise, particularly when compared to the exact science of measuring a supply of electricity. Second, even if such measurement problems could be adequately solved, it would be simply impossible to "supply" a vertical tranche of energy efficiency (which presumably would be a constant portion of load in every hour of the year that has been reduced). Hence, the provision of energy efficiency resources cannot be adequately compared against the supply of vertical tranches in a manner that would enable them both to be treated interchangeably in the same auction.

(*Id*., p. 27, lines 559-569)

Based on the above-summarized record evidence, Staff respectfully recommends that the Commission take no action in this docket to order the Ameren

Companies or potential suppliers to include renewable power or energy efficiency resources in their supply portfolios.

B. Additional other issues

Staff reserves the right to respond in its reply brief to parties who address this matter in their initial briefs.

X. CONCLUSION

WHEREFORE, for all the reasons set forth herein, the Staff of the Illinois Commerce Commission respectfully requests that its recommendations be adopted in this proceeding.

Respectfully submitted,

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