ILLINOIS COMMERCE COMMISSION

DOCKET NOS. 06-0070, 06-0071, & 06-0072

REBUTTAL TESTIMONY

OF

C. KENNETH VOGL

Submitted On Behalf

Of

CENTRAL ILLINOIS PUBLIC SERVICE COMPANY d/b/a AmerenCIPS,

CENTRAL ILLINOIS LIGHT COMPANY d/b/a AmerenCILCO,

ILLINOIS POWER COMPANY d/b/a AmerenIP

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C. KENNETH VOGL

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I. INTRODUCTION

Q. Please state your name and business address.

A. My name is C. Kenneth Vogl. My business address is 101 South Hanley, Suite 900, St. Louis, Missouri 63105.

Q. Are you the same C. Kenneth Vogl who submitted testimony in these proceedings?

A. Yes I am.

II. PURPOSE OF TESTIMONY

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to rebut portions of the testimony submitted by Peter Lazare, David J. Effron, Alan Chalfant, and James T. Selecky. Specifically, each of the individuals listed above address issues related to pensions and/or OPEBs in their testimony. Some individuals address pension and OPEB issues directly and some individuals address pension and OPEB issues indirectly as a part of A&G expenses. My testimony will focus on the pension and OPEB issues that are referred to in each individual's testimony.

III. REBUTTAL TO PETER LAZARE TESTIMONY

Q. Please summarize the portion of Mr. Lazare's testimony that you are rebutting with respect to pension and/or OPEB issues.

A. Mr. Lazare addresses pension and OPEB issues indirectly through his comments regarding A&G expenses. He comments that increases in A&G expense are unreasonable and he does not understand why the Companies can control direct expenses but not A&G expenses.

Q. Do you agree with Mr. Lazare's statement included in lines 437 – 439 of his testimony: "The Ameren Companies have failed to explain why increases in A&G expenses ranging from 63% to 394% (or 210% on a collective basis) are necessary"?

A. As an expert on pension and OPEB issues, I disagree with Mr. Lazare regarding the pension and OPEB components of A&G expenses. I believe that Mr. Lazare calculates his percentage increases by comparing the amounts approved in the last rate case for each company to the amounts reflected in the pro forma test year. I do not believe this is a meaningful comparison. Moreover, I can explain both why the increases in pension and OPEB have occurred and why the pro forma levels accurately reflect the Ameren Companies' actual expenses. The table below shows previously approved levels of pension and OPEB expenses and the pension and OPEB expenses in the pro forma test year.

	Prior Order	**Proposed**	**Increase**
Pension	$ (8,866,530)	$ 22,836,985	$ 31,703,515
OPEB	5,008,524	24,163,221	19,154,697
Total	$ (3,858,006)	$ 47,000,206	$ 50,858,212

Please note that a significant portion of the increase in A&G expenses that Mr. Lazare focuses on is driven by increases in both pension and OPEB expenses (i.e., $50.9 million out of $102.6 million).

I explain, in my direct testimony, the key factors driving the increases in pension and OPEB expenses since the prior order, thereby explaining the reasons for a large portion of the increase in A&G expenses. Specifically, I showed that interest rates, returns on equity investments, and medical inflation were the key drivers of the increase in pension and OPEB expenses.

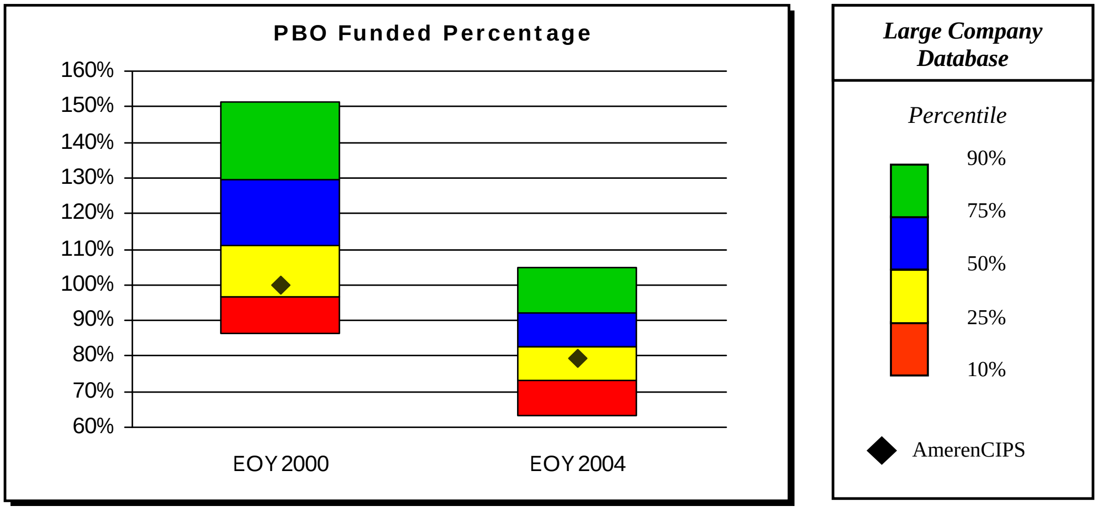
Finally, because pension and OPEB expenses represent a large portion of the increase of A&G expenses (i.e., 49.6% of the total increase), the percentage increase in A&G expenses (i.e. 210% on a collective basis per Mr. Lazare's testimony) is skewed by the pension and OPEB expenses and does not provide a reasonable measure of the increase in other A&G expenses. A better – and more realistic – measure would be to determine the increase in other A&G expenses net of pension and OPEB expenses.

Q. Please explain your rationale for determining the increase in A&G expenses net of pension and OPEB.

A. Clearly, pension benefits are a valuable component of any benefit program and are not free. As I describe in my direct testimony, pension (FAS 87) and OPEB (FAS 106) expense can be described as: (1) the value of benefits earned during the year (i.e., service cost), plus (2) a charge or credit depending on the funded status of the plan (i.e., interest cost less return on assets), plus (3) a charge or credit to recognize special asset and liability changes (i.e., amortization). Because pension plans were overfunded at the time of the prior order, pension expense became negative reflecting the impact surplus assets have on FAS 87 pension expense. Even though OPEB plans were not overfunded at the time of the prior order, they were less underfunded and OPEB expense was much lower. With declining interest rates and the relatively poor market performance since the prior orders, pension plans today are generally underfunded and OPEB plans are more underfunded than they were at the time of the prior orders. A reasonable expense for these plans should now reflect 1) the value of benefits earned during the year, plus 2) a charge to reflect the underfunded status of the plan. As a result, it would be more appropriate to exclude increases in pension and OPEB expenses when evaluating the increase in controllable A&G expenses.

Q. Please comment on Mr. Lazare's following statements included in lines 460 – 463 of his testimony: "The significantly higher rate of increase for A&G expenses would indicate that the success the Ameren Companies contend they are realizing in controlling direct expenses is not carrying over to A&G expenses. It is not evident why the Ameren Companies can control one set of costs but not another.".

A. Once again, as an expert on pension and OPEB issues, I described in my direct testimony that factors beyond the control of Ameren (i.e., interest rates, returns on equity investments, and medical inflation) were the key drivers of the increase in pension and OPEB expenses since the prior order.   Moreover, I explained how Ameren's results did not diverge from general industry experience in any material respect. In other words, as compared to other large companies, Ameren did not do a substandard job in managing its pension and OPEB costs. As support for this point, the chart below shows the distribution of pension plans' funded percentages as of the end of 2000 and the end of 2004. AmerenCIPS's actual funded percentage is also shown and indicates AmerenCIPS's experience has been fairly consistent with other companies. The distribution of other companies' funded percentages shows the median pension plan funded percentage has dropped 25% – 30% over the last five years which in turn has caused the significant increases in pension expense. AmerenCIPS's funded percentage has dropped 20% over the same period. Please see my direct testimony which illustrates the same point for the other Ameren Companies.



Please note that the information in the above chart is taken from the Towers Perrin Large Company Benchmark Database which includes over 200 companies in 30 or more different industries. The information has been gathered from the publicly disclosed annual report of each company.

Therefore, since increases in pension and OPEB expenses represent such a large portion of the increase in A&G expenses (i.e., $50.9 million out of $102.6 million), this explains why the increase in A&G expense is largely beyond the control of Ameren.

IV. <u>REBUTTAL TO DAVID J. EFFRON TESTIMONY</u>

Q. Please summarize the portion of Mr. Effron's testimony that you are rebutting with respect to pension and/or OPEB issues.

A. Mr. Effron suggests in his testimony that the accrued OPEB liability be deducted from rate base. In lines 14 – 16 of page 8 of his Illinois Power testimony, Mr. Effron states "The accrued OPEB liability represents the excess of OPEB expense recorded by the Company over the amounts actually paid, in other words, 'ratepayer-supplied OPEB funds'." His reasoning is that the accrued OPEB liability represents ratepayer-supplied

OPEB funds that are in the control of the Company, and should therefore be deducted from rate base.

Q. Do you agree with his description of accrued OPEB liability?

A. No. The accrued OPEB liability is the excess of OPEB expense recorded by the Company (a non-cash expense recorded by the Company on its income statement) over the amounts the Company has actually paid for OPEB. It does not necessarily represent ratepayer supplied funds that the Company intends to use for OPEB.

Q. Do you agree that the accrued OPEB liability should be deducted from rate base?

A. No. As I understand it, rate base is intended to represent the net investor-supplied capital dedicated to public utility service. Mr. Effron's contention is that ratepayers have supplied funds in excess of what the Company has paid for OPEB, and that the excess is available to support the Company's operations. Thus, in Mr. Effron's view, that excess should be deducted from rate base as a non-investor supplied source of funds. The problem with Mr. Effron's position is not his understanding of what rate base represents, but rather, his arithmetic. I agree that, as a matter of ratemaking theory, any rate base adjustment for OPEB, positive or negative, should equal the excess or shortfall of the amount the Company has collected in rates for OPEB over or under the amount the Company has actually paid for OPEB. However, there is no excess. For example, at AmerenCIPS, the OPEB expense included in the prior order was roughly $0.8 million; the OPEB contributions, before allocations for O&M, electric, etc., were roughly $55 million from 1999 through 2004' and the cumulative FAS 106 expense, before allocations, over the same period was roughly $57 million. Even though a small accrued OPEB liability exists, Ameren has contributed far more for OPEB than it has collected from ratepayers. Therefore, if an adjustment to rate base was made, the correct adjustment would be an increase to rate base equal to the excess of OPEB funds contributed over the amount collected in rates from ratepayers.

V. REBUTTAL TO ALAN CHALFANT TESTIMONY

Q. Please summarize the portion of Mr. Chalfant's testimony that you are rebutting with respect to pension and/or OPEB issues.

A. Mr. Chalfant addresses pension and OPEB issues indirectly through his comments regarding A&G expenses. He comments that A&G expense should increase in proportion to any authorized increase in other (non-A&G) O&M expense.

Q. Please respond to Mr. Chalfant's recommendation for rate recovery of A&G expenses that he discusses in lines 215 – 218 of his testimony, specifically, "To the extent the commission approves increased amounts of O&M expense for the adequate provision of delivery service, the amount of overhead or A&G should be increased proportionally."

A. In my rebuttal to Mr. Lazare's testimony, I discussed the reasons for the large increase in pension and OPEB expenses, which represent 49.6% of the increase in A&G expenses since the prior order. The pension (FAS 87) and OPEB (FAS 106) expenses included in the current case reflect the expenses of Ameren's underfunded plans, and these expenses are reasonable compared to pension and OPEB expenses for similarly sized organizations. However, the pension and OPEB expenses included in the prior orders for the Ameren Companies reflected the Ameren plans at a time when they were more fully funded, as a result of then current economic environment. In fact, the pension plans were overfunded. Due to subsequent investment performance, the plans have become underfunded and there has been a significant increase in pension and OPEB expenses. As stated previously, the increases in pension and OPEB expenses are primarily the result of changes in interest rates, returns on equity investments, and medical inflation. As such, these increases are unlikely to be correlated to any increase in O&M expense, which are not generally subject to the same pressures and drivers.

VI. <u>REBUTTAL TO JAMES T. SELECKY TESTIMONY</u>

Q. Please summarize the portion of Mr. Selecky's testimony that you are rebutting with respect to pension and/or OPEB issues.

A. Mr. Selecky notes in lines 698-699 of his testimony that pension and OPEB expense "represent a significant portion of the requested A&G expense". Furthermore, because the pension and OPEB expense has been increasing over the past several years, in lines 727-729 he is "recommending that the ICC approve a normalized level of pension and OPEB expenses to be included in Ameren Utilities' revenue requirements". His approach averages the past five years of pension and OPEB expenses to determine the normalized expense amounts. Mr. Selecky claims that this is a reasonable approach.

Q. Do you believe that this approach is reasonable?

A. First, in my opinion, a reasonable approach for rate recovery of pension and OPEB expenses would allow for the full recovery of these expenses over time (i.e., no more or no less). As I discussed in my direct testimony, and as Mr. Selecky agrees, pension and OPEB expenses can be very volatile. Mr. Selecky's proposed approach normalizes the peaks (high cost periods) while ignoring the valleys (low cost periods). In my opinion, this approach is not reasonable because it would result in less than full pension and OPEB expenses being reimbursed by ratepayers. It is important to note that the pension and OPEB expenses approved in the prior orders were very low. These prior orders' expenses for 1999 or 2000 reflect expenses for overfunded plans that were generated by the high equity returns during the late 1990s. In essence, the change in pension and OPEB expense since the prior orders simply reflects the adjustment in economic environment.

Secondly, the pension and OPEB expenses for any given year should be equal to the benefits earned in that year plus an adjustment based on the funded status of the plan. Note that all publicly-held companies calculate their pension and OPEB expense using FAS 87 and FAS 106, which are both in accordance with Generally Accepted Accounting Principals. Since both FAS 87 and FAS 106 determine expense for the pension and OPEB plans in this manner, these expenses should be reimbursed by ratepayers on the same basis. (Please refer to my direct testimony for more detailed information on the calculation of FAS 87 and FAS 106 expense.) Using this approach ensures that the pension and OPEB expense for any given year is tied to the current funded position of the plans. In my opinion, it is unreasonable to normalize the pension and OPEB expense so the costs are not representative of the current funded position. Mr. Selecky's approach would yield pension and OPEB expenses that are significantly different than the current funded position of the plans suggest.

VII. <u>SUMMARY</u>

Q. Would you like to briefly summarize your testimony?

A. Yes. Peter Lazare, David J. Effron, Alan Chalfant, and James T. Selecky each submitted testimony containing issues directly or indirectly pertaining to pension and/or OPEB benefits. My testimony rebuts certain portions of their testimony that address pension and/or OPEB treatment.

In rebutting Mr. Lazare's testimony, I have shown that the increases in pension and OPEB expenses are reasonable. In addition, I have shown that the key factors that drove the pension and OPEB expense increases were largely out of Ameren's control.

In rebutting Mr. Effron's testimony, I have shown why I do not agree with the deduction from rate base he is recommending. I describe my approach and the corresponding rate base adjustment.

In rebutting Mr. Chalfant's testimony, I have shown that the increases in pension and OPEB expenses are not necessarily in proportion to the other (non-A&G) O&M expense.

In rebutting Mr. Selecky's testimony, I have shown why I believe his recommended approach to normalize pension and OPEB expense is unreasonable.

Q. Does this conclude your testimony?

A. Yes, it does.

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