STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Central Illinois Light Company d/b/a AmerenCILCO **Proposed general increase in rates for delivery service (tariffs filed December 27, 2005)**	**)**	**Docket No. 06-0070** **(Cons.)**
Central Illinois Public Service Company d/b/a AmerenCIPS **Proposed general increase in rates for delivery service. (tariffs filed December 27, 2005)**	**)**	**Docket No. 06-0071**
Illinois Power Company d/b/a AmerenIP **Proposed general increase in rates for delivery service (tariffs filed December 27, 2005)**	**)**	**Docket No. 06-0072**

REPLY BRIEF OF THE STAFF OF THE ILLINOIS COMMERCE COMMISSION

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STAFF OF THE ILLINOIS COMMERCE COMMISSION

Staff of the Illinois Commerce Commission ("Staff"), by and through its undersigned 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 Reply Brief in the above-captioned matter.

INTRODUCTION

The Initial Brief of the Staff of the Illinois Commerce Commission ("Staff's Initial Brief" or "Staff IB") was filed on August 23, 2006. The Initial Brief Of The People Of The State Of Illinois ("AG's Initial Brief" or "AG IB"), the Initial Post-Hearing Brief of the

Ameren Companies ("Ameren's IB" or "Ameren IB"), the Initial Hearings Brief For Cities of Champaign, Urbana, and Bloomington, Town of Normal and Champaign County; the Initial Brief Of Constellation NewEnergy, Inc. and Peoples Energy Services Corporation ("CNE/PES Initial Brief" or "CNE/PES's IB"), the Initial Brief Of The Citizens Utility Board ("CUB's IB" or "CUB IB"), the Initial Brief Of Illinois Industrial Energy Consumers ("IIEC's Initial Brief" or "IIEC IB"), the Initial Brief Of Local Unions 51, 309, 649, 702, and 1306 of the International Brotherhood of Electrical Workers, AFL-CIO ("IBEW's IB" or "IBEW IB"), the Initial Brief of the Kroger Co. ("Kroger's IB" or "Kroger IB"), and the Initial Brief of Wal-Mart Stores, Inc. ("Wal-Mart's IB" or "Wal-Mart IB") were also filed on August 23, 2006.

Some of the issues raised in the parties' initial briefs were addressed in Staff's Initial Brief and, in the interest of efficiency, Staff has not raised or repeated every argument or response previously made in Staff's Initial Brief. Thus, the omission of a response to an argument that Staff previously addressed simply means that Staff stands on the position taken in Staff's Initial Brief because further or additional comment is neither needed nor warranted.

ARGUMENT

I. RATE BASE

A. Summary of Uncontested/Settled Issues

B. Plant Additions

In its Initial Brief, the Ameren Companies claim that Staff's proposed disallowances of costs related to historic plant additions are related "solely to disputes over documentation of the Ameren Companies' reasonably incurred costs". (Ameren IB, p. 1) The simple fact of the matter is that, when asked to do so, the Ameren

Companies failed to verify that the costs in question were actually incurred or were for the purpose indicated. When seeking appropriate verification of these costs, Staff requested information that the Ameren Companies should have had in their possession pursuant to the Commission's record retention rules (83 Ill. Adm. Code 420). Staff evaluated all the documentation the Companies did provide and disallowed costs for which information was found to be lacking. The Companies left Staff no other alternative in this matter.

The Ameren Companies try to redirect the Commission's attention away from the central issue by claiming that Staff's adjustment should be rejected because it contains mathematical errors. Put simply, the evidence demonstrates otherwise. The "mathematical error" Ameren claims with regard to CILCO work order 3648 (Ameren IB, p. 2) was clearly shown to be an error in Ameren's own effort to provide documentation in excess of costs actually disallowed by Staff. (Staff IB, pp. 7-8) Likewise, the Companies' attempt to provide purchase orders as support for past expenditures (Ameren IB, pp. 3-4), rather than actual invoices or other documentation supporting the actual final historic costs incurred, was shown to be improper support. (Staff IB, pp 8-9)

Further, the Ameren Companies' Initial Brief regarding AmerenIP's work order 25438 is simply incomprehensible and is in no way a "mathematical error" as they claim. In a statement filed on e-docket on August 17, 2006, the Companies acknowledged that they had not provided support and would face the consequences of that action. Specifically, paragraph 9 of the Companies' statement reads as follows:

> The Ameren Companies regret this error. They do not seek to supplement the record at this time with any information that they could have provided earlier. They feel compelled, however, to correct Mr. Stafford's

> inadvertently erroneous statements, and accept the consequences of their error.

(Statement of the Ameren Companies filed on e-docket on August 17, 2006, p. 3) Now, rather than face those consequences, the Companies disingenuously argue their failure to provide support is a "mathematical error" by Staff; thus, effectively recanting their admission. They continue to claim that "full support" was provided for AmerenIP work order 25438 (Ameren IB, p. 4) contrary to its own acknowledgement that said "full support" was not provided. Indeed, Ameren admits that Mr. Stafford's testimony, cited in the its Initial Brief, as well as Ameren Ex. 36.10, Schedules 1, 2 and 3, all contain certain information not supported in the record. While the Companies did not "seek to supplement the record" for the information not provided, they now attempt to do just that by claiming all costs associated with this work order have been "fully supported". Simply put, the Ameren Companies' assertions in its Initial Brief are inconsistent with the record.

The Ameren Companies continue to misrepresent Staff's adjustment as resulting in negative Utility Plant in Service for Account 303 and for Intangible Plant in Service. Ameren presents its own version of Staff's adjustment on Respondents' Exhibit 36.13. . (Ameren IB, p. 5) In doing so, Ameren misconstrues Staff's adjustment. As already discussed in Staff's Initial Brief, Ameren witness Stafford acknowledged during cross examination that Staff's adjustment was made to utility plant in service and not to any individual plant account or group of accounts. (Staff IB, pp. 9-10) Staff's response to Ameren Data Request 14.12 cited by the Companies (Ameren IB, p. 5) only further supports Staff's position that it has not in the past and is not currently proposing a negative balance for gross utility plant in service.

The Commission should accept Staff's adjustment to plant additions. Staff's proposed adjustment is consistent with the supporting documentation provided to Staff by the Ameren Companies. The Companies acknowledge that they have erred in providing full support and state they "accept the consequences of their error". (Statement of the Ameren Companies filed on e-docket August 17, 2006)

C. Pro forma Plant Additions

The rate case test year guidelines (83 Ill Adm. Code Section 287.40) state that "Any proposed known and measurable adjustment to the test year shall be individually identified and supported in the direct testimony of the utility". The Ameren Companies failed to provide the required support in their direct testimony. However, in this proceeding, Staff considered support the Companies provided as late as the Companies' rebuttal testimony, clearly beyond what is required by Part 287.

The Companies incorrectly argue that "they have provided sufficient justification and support for full recovery of the actual costs in the amount of $12.131 million" for the Ameren IP pro forma adjustment. (Ameren IB, p. 6) First, the $12.131 million is the total amount of the project and does not reflect the Electric Distribution portion; thus, full recovery of $12.131 million is not appropriate in any event. Second, the additional information Ameren provided with its surrebuttal testimony on which it wishes to rely for its adjustment was stricken by the Administrative Law Judges in granting in part Staff's Motion to Strike Certain Testimony filed on e-docket on July 18, 2006. (Tr., p. 370)

In its Initial Brief, Staff did revise its adjustment for the IP pro forma plant adjustment to base it on the amount of costs supported by Ameren, rather than subtracting unsupported costs from the amount proposed by the Companies. (Staff IB, pp. 11-12) While Staff's calculation differs from that described by Ameren (Ameren IB, p. 7), the calculations would both seem to yield the same result. Therefore, it appears to Staff that Ameren would not be opposed to Staff's revised adjustment.

D. G&I Plant

1. Functionalization of Plant

The arguments presented by the Ameren Companies fail to provide any reasonable basis for their proposed levels of G&I plant. Instead, they serve to underscore the reasonableness of Staff's proposed adjustment of these plant balances.

The Companies begin by arguing that G&I plant is for the most part distribution-related. They state as follows:

> Historically, while some of the G&I plant assets were used by and benefited more than one line of business, the assets primarily benefited the 'pipes and wires" businesses. For example, the land and structures that have been recorded as G&I plant represent discrete assets that can be identified and assigned or allocated to specific lines of business. The vast majority of the assets in those accounts are district field facilities that house field operations personnel and have not provided support to the electric production business. Accordingly, it would be inappropriate to assign or allocate a portion of these G&I plant assets to the electric production business.

(Ameren IB, p. 7) This argument is fundamentally flawed. It consists of unsupported assertions that are not tied to the record in any way. For example, the Companies' claim that G&I plant primarily benefits the "pipes and wires" business is far from an established fact. The Commission, for one, has reached a different conclusion in previous cases and allocated a larger share of G&I plant to generation (*See* ICC Docket No. 99-0117 (ComEd) Order dated August 26, 1999, p. 11; ICC Docket No. 01-0423 (ComEd) Order dated March 28, 2003, p. 41; ICC Docket Nos. 99-0129 & 99-0134 (Illinois Power) Order dated August 25, 1999, p. 30; ICC Docket No. 01-0432 (Illinois

Power) Order dated March 28, 2002, pp. 17-18; ICC Docket No. 99-0121 (AmerenCIPS and AmerenUE) Order dated August 25, 1999, p. 21).

The Companies go on to identify perceived problems with the alternative approach of a labor allocator that was employed in previous cases for vertically integrated Ameren Companies to determine G&I plant balances. The Companies employ a hypothetical example in their effort to undermine the labor allocator approach. Under the Companies' example, if the Companies invest in a software system which reduces the level of distribution employees, the labor allocator will functionalize more of that system's costs to generation despite the fact that it is distribution-related. (Ameren IB, p. 9)

It is always possible to construct a hypothetical example that can identify a flaw in an allocation methodology. That the Company has done so in its initial brief is beside the point. The key issue concerns not whether the labor allocator approved by the Commission in previous cases is beyond reproach, but whether it is a more reasonable functionalization approach than the alternative presented by the Ameren Companies. The available evidence indicates that to be the case. In previous cases, the Commission has lent its support to the labor allocator and specifically rejected the alternative asset separation methodologies based on the direct assignment approach proposed by Ameren Companies. (*See* ICC Docket No. 99-0134, Order at 16). Furthermore, Staff has identified additional shortcomings in the ASP which is the current version of the Companies' direct assignment approach. (Lazare Dir., ICC Staff Exhibit 6.0, pp. 10-12) Thus, while the labor allocation methodology adopted by the Commission in previous cases is less-than-perfect, it is far superior to the functionalization approach proposed by the Companies in this case for the reasons explained by Staff.

The Ameren Companies then seek to bolster their own functionalization approach, the Asset Separation Project (ASP). They argue that the ASP is the superior approach because it incorporates the more accurate direct assignment methodology to functionalize costs. According to the Companies, the ASP begins with the assets of the three Companies and then employs a combination of direct assignments and allocators to functionalize each Company's G&I plant to distribution. (Ameren IB, pp. 9-11)

The explanation provided by the Companies cannot overcome a fundamental flaw in the ASP approach. That flaw lies with the starting point for their analysis, the G&I plant balances for the three Companies. Those balances are simply not meaningful from the standpoint of functionalizing G&I plant. The Companies have restructured in recent years and divested their generation assets. As a result, the G&I balances for the three Ameren Companies consist solely of plant that has already been functionalized to transmission and distribution. The functionalization of G&I plant to generation, which was a critical issue in previous delivery service cases, falls outside the realm of the Companies' analysis. Thus, the Ameren Companies have failed to demonstrate that G&I plant has been equitably allocated between the regulated utility and Ameren's unregulated generation subsidiaries in this docket. The absence of this analysis represents a fundamental shortcoming that undermines the validity of Ameren's ASP methodology. (Lazare Dir., ICC Staff Exhibit 6.0, pp. 11-12)

Furthermore, the Companies' functionalization process has reallocated to the regulated transmission and distribution utilities G&I plant that the Commission previously determined to be generation-related. Nevertheless, the Ameren Companies have failed to provide for the record any evidence to indicate that these assets should be reallocated from generation to delivery services. Instead, the Company have presented without explanation a set of G&I plant balances for the restructured transmission and distribution utilities and then determined the distribution share of those balances using the ASP approach. In short, the Companies arbitrarily reallocated back to distribution G&I plant that the Commission determined was not distribution-related in the previous round of delivery service cases. The Companies' actions are ill-conceived and inappropriate and should be rejected by the Commission. (*Id***.**, p. 13)

The Companies also find fault with the proposed adjustments to G&I plant presented by Staff and the IIEC. They argue as follows:

> Notwithstanding the clear evidence to the contrary, both the Staff and IIEC proposed adjustments to G&I plant. Notably, neither party challenged any particular element of the Companies' study. Nor did they question the prudence or used and usefulness of any specific plant item wholly or partially included in rate base. Rather, their adjustments – while arrived at by different paths – were based on the Commission's Orders in each Company's last delivery service tariff ("DST") proceeding. As will be discussed, to adopt the position of Staff and IIEC, the Commission must conclude, despite all evidence to the contrary, either that: (i) the G&I plant assets on the utilities' books are being used by the Companies' affiliates' non-regulated generation businesses, or (ii) the assets are not being used in support of the Companies' regulated electric businesses. Neither of these propositions is correct.

(Ameren IB, pp. 11-12) The above passage encapsulates the flaws in the Companies' arguments on this issue. It begins with the erroneous claim that Staff has not challenged any particular element of the Companies' ASP study. In fact, Staff has consistently criticized the ASP for being narrowly focused and failing to include generation subsidiaries in the functionalization process. (Lazare Dir., ICC Staff Exhibit 6.0, pp. 11-12)

Second, the passage shows how the Companies seek to shift the burden of proof on this issue by arguing that Staff and IIEC have the responsibility to demonstrate that the specific G&I plant assets at issue support the non-regulated generation function. This argument is patently unreasonable because the burden on this issue clearly lies with the Companies. In this proceeding they seek to restore to rate base G&I plant that the Commission specifically removed in the last round of delivery service cases. The Companies must show why those previous decisions should be reversed in the current case. However, they have fallen woefully short of meeting that burden. This is reason enough alone for the Commission to continue to exclude this plant from distribution rate base by accepting Staff's proposed G&I plant adjustment. (Lazare Reb., ICC Staff Exhibit 17.0, pp. 9-10)

The Companies also seek to rebut the Staff argument that the "Companies are attempting to refunctionalize this [G&I] plant back to the revenue requirement". (Ameren IB, p. 13) They argue as follows:

> The Companies' ASP reflects the actual assets which were on the books as of December 31, 2004 and how such assets are used by the Companies to provide service to its customers. The G&I plant which has been included in the Companies' rate base in these proceedings reflect the plant that is used by the electric delivery services business. The Companies transferred the G&I plant which supported the non-regulated generation business to those businesses. Therefore, the Companies are not attempting to refunctionalize plant back to the electric distribution business but rather is accurately reflecting how the assets are used and attempting to earn a fair return on those assets which are used by the electric distribution business from the customers which benefit from the use of such assets.

(*Id.*, pp. 13) There is a fundamental flaw in the Companies' argument. The problem lies with the starting point for their functionalization process which they indicate is the plant used by the electric delivery services business. According to the Companies, these balances were developed by transferring away the G&I plant supporting the non-regulated generation businesses. In other words, the Companies decided on their own which G&I plant assets should be allocated to the generation subsidiary and which should remain with the transmission and distribution utility. Then, they present a limited analysis to the Commission that divvies up G&I plant between the transmission and distribution functions.

It should be remembered that Ameren transferred far less G&I plant to the non-regulated generation business for this case than the Commission functionalized to generation when it was part of the vertically integrated utility. Since the Commission refused to functionalize G&I plant in the manner the Companies want, they have refunctionalized this plant on their own without explanation, and now seek to present the Commission with a fait accompli. This action is clearly inappropriate and should be rejected by the Commission. (Lazare Dir., ICC Staff Exhibit 6.0, pp. 12-13)

Finally, the Companies criticize Staff for failing in its proposed adjustment to recognize the further amortization or depreciation of G&I plant assets on the Companies' books as of December 31, 1999 or 2000. (Ameren IB, p. 15) They go on to argue that recognition of this depreciation would significantly reduce the magnitude of Staff's proposed adjustment. (*Id.*)

As noted in Staff's Initial Brief, this argument is clearly poorly timed. Staff presented its adjustment in direct testimony, but the Company did not challenge the reasonableness of the calculation until surrebuttal that was filed only a few days before hearings. That left insufficient time for Staff to evaluate the basis for the Company's alternative calculation. The Companies' last minute effort to confuse the record should be rejected by the Commission as clearly inappropriate.

2. Plant transfer

3. G&I Plant Amortization

E. Reallocation of Depreciation Reserve

AmerenIP continues to extol the virtues of reallocating its depreciation reserve (i.e., accumulated depreciation) in what Staff views as a transparent effort to make it appear that it has done something useful with the depreciation study that it wants the ratepayers to pay for as part of rate case expense in the current proceeding. (*See* Ameren IB, pp. 17-19) The reallocation of the depreciation reserve was not proposed until Staff took issue with AmerenIP's proposal to include the cost of the depreciation study in rate case expenses. AmerenIP ignores the fact that the Statement of Financial account Standards ("FAS") 71 that it cites as supportive of the reallocation (Stafford Sur., Respondents' Exhibit 36.0, p. 17) merely specifies how the effects of different types of rate actions are reported in general-purpose financial statements. There is nothing to indicate that reallocation of the depreciation reserve is acceptable under the rules of GAAP. (Jones Reb., ICC Staff Exhibit 14.0, p. 9)

The Company also ignores the fact that the reallocation does nothing to correct the problem of inaccurate depreciation rates. (*Id*., p. 8) The depreciation study indicated a large disparity in the actual vs. the calculated depreciation reserve. (Stafford Sur., Respondents' Exhibit 36.0, p. 18) The depreciation study also indicated a substantial increase in depreciation rates for AmerenIP. (*Id*., p. 15) Presumably; the inaccurate depreciation rates are the cause of the disparity in the depreciation reserve and will continue to be so until corrected. Reallocating depreciation reserves would have no impact on AmerenIP's revenue requirement in the current rate proceeding. (Tr., p. 492) Ameren's claim that the reallocation will mitigate the future impact of changes in depreciation rates to customers (Ameren IB, p. 18) is not meaningful. Just as shuffling accumulated depreciation among the individual depreciable asset groups does not change the total amount of accumulated depreciation, neither does it change the total amount of depreciation expense that will eventually be recovered for those asset groups.

Staff recommends that the Commission deny AmerenIP's request to reallocate its depreciation reserve because (1) reallocation does nothing to correct the problem of inaccurate depreciation rates and (2) there is nothing to indicate that the methodology is acceptable under GAAP. Finally, it appears that the real reason AmerenIP is proposing the reallocation of its depreciation reserve is to justify recovery from ratepayers.

F. OPEB Liability

1. Unfunded OPEB

The Ameren Companies' arguments against reducing rate base by the unfunded OPEB liability at December 31, 2004 (Ameren IB, pp. 19-24) are unconvincing and demonstrate a lack of understanding of the ratemaking process. One cannot simply identify the amount of OPEB expense included in the cost of service on which current rates are based and state that is the amount the Ameren Companies have recovered each year that the rates have been in effect. (Ameren IB, p. 22)

It is inappropriate from an accounting perspective to single out any particular component of the cost of service and analyze that item in isolation. The cost of service must be considered in the aggregate. The components of cost of service are dynamic, in that the costs of some things increase, while the costs of other things decrease. The appropriate comparison is to compare what has been expensed with what has been funded. The OPEB liabilities reflect that the Ameren Companies have recorded more OPEB expense than they have actually paid. (Jones Reb., ICC Staff Exhibit 14.0, p. 19)

Because OPEB expense is provided for in base rates, the unfunded liability reflects a cost-free source of capital on which shareholders are not entitled to receive a return. (*Id*.) Company witness Vogl claims that the OPEB liability does not necessarily represent ratepayer supplied funds. (Vogl Reb., Respondents' Exhibit 21.0, p. 6) As AG witness Effron points out, Mr. Vogl fails to explain how the accrued OPEB liabilities in these proceedings differ from the accrued OPEB liabilities in Docket Nos. 95-0219 and 04-0779, wherein the Commission described the accrued OPEB liability as representing ratepayer supplied funds that should be deducted from rate base. (Effron Reb., AG Exhibit 3.0, p. 2)

The adjustment to reduce rate base by the accrued OPEB liability at December 31, 2004 is appropriate and should be adopted by the Commission.

2. ADIT Treatment

Contrary to the Ameren Companies' position, the Accumulated Deferred Income Taxes ("ADIT") related to the OPEB liability should not be removed from rate base. (Ameren IB, pp. 24-25) To be consistent with the inclusion of the OPEB liability in rate base, the related ADIT must also be included in rate base.

If the Commission adopts the adjustment to reduce rate base by the accrued OPEB liability, it should also adopt this adjustment to reflect the related ADIT in rate base.

G. Cash Working Capital

The AG incorrectly characterizes the uncontested status of the issue regarding the treatment of Federal and FICA withholding taxes as they impact the cash working capital ("CWC ") allowance. (AG IB, pp. 2-3) While the quoted testimony is not inaccurate, Ameren witness Adams accepted *Staff's* position on this component of CWC during evidentiary hearings on July 25, 2006. (Tr., pp. 529 – 530) Ameren also indicates that this issue was resolved at hearing. (Ameren IB, p. 35) The AG has not commented on Staff's position presented in Staff witness Ebrey's rebuttal testimony. (ICC Staff Exhibit 13.0 (Corrected), pp. 14-16) Thus, while Ameren and Staff are in agreement on the treatment of payroll withholding taxes, the AG's opinion of Staff's position is unknown.

1. Lead/lag methodology

The Ameren Companies continue to make the same unfounded arguments regarding their respective CWC allowances. The Companies claim that "until this case, the Staff has argued hard for the Net Lag approach" but fail to cite any cases where Staff made such an argument. (Ameren IB, p. 27)[1] While Staff suggested that the Net Lag approach may be more appropriate in the last Ameren gas rate case, Docket Nos. 02-0798/03-0008/03-0009 (Cons.), Staff's position in that case was that the Companies

[1] Staff notes that Section I.G. of the Ameren IB appears to cite the testimony of Ameren witness Stafford (Ameren Ex. 16.0) instead of the testimony of Ameren witness Adams (Respondents' Exhibit 17.0), who actually testified with respect to the Cash Working Capital Calculation.

had not supported the level of cash working capital it had requested. (ICC Staff Exhibit 13.0 (Corrected), p. 6) This position can hardly be described as having been "argued hard for the Net Lag approach". Ameren cites no other cases in which Staff supposedly made such an argument.

The Ameren Companies cite three reasons why it adopted the Net Lag methodology to determine its CWC requirements. (Ameren IB, p. 28) The Commission should be persuaded by none of these. First, the Companies argued that they wanted to "ensure consistency across all the companies". (*Id*.) Staff agrees with this goal and Staff did consistently use its proposed method, the Gross Lag methodology, for all the Companies in this proceeding. However, the Companies' argument fails to establish the superiority of one method over another, and that is the issue at hand.

The Companies' second and third reasons to adopt the Net Lag methodology (the methodology has been accepted in both state regulatory jurisdictions in which the companies operate and most state regulatory jurisdictions have adopted the Net Lag approach, respectively) are unsupported in the record. (*Id.*) In fact, the ALJ's invited the Companies to cite just such information in its Initial Brief. (Tr., p. 370) Having failed to provide that information, the statements are unsupported and should be given no weight in the final determination on this issue.

The Ameren Companies also argue that the iterative nature of the Gross Lag Methodology increases the difficulty of calculating the CWC requirements for each Company. (Ameren IB, p. 29) Staff noted that both the Gross Lag and Net Lag methodologies are iterative in nature, citing Ameren witness Adams' own acknowledgement that even using his methodology, certain modifications will be needed in the determination of the final CWC requirement. (Ebrey Reb., ICC Staff Exhibit 13.0 (corrected), p. 8) Likewise, Ameren witness Stafford agreed that certain expense levels in the final determination of the CWC requirement were dependent upon the final revenue requirements determined in this proceeding. (Tr., pp. 434-436, 444-445, and 453; Staff IB, p. 37)

Just as the level of the various cash expenses are used to determine the CWC requirement, so also must the level of cash revenues provided by ratepayers be considered. (Ebrey Reb., ICC Staff Exhibit 13.0 (Corrected), p. 5; Staff IB, p. 30) The Ameren Companies have never rebutted this statement. In fact, the Companies admit through their Initial Brief that the Net Lag methodology does not include revenues. (Ameren IB, pp. 29 and 30) As Staff witness Ebrey stated during cross examination,

> To the extent that the daily cash provided through base rate revenues exceeds the daily cash needs of the company, those funds are ratepayer-supplied and result in negative cash working capital.
>
> When the daily cash provided through base rate revenues is less than the daily cash needs of the company, the shortfall [is] with shareholder supply then results in positive cash working capital.

(Tr. 559-560) Without any measure of the **amount** of revenues provided by the ratepayers, the amount, if any, to be provided by shareholders cannot be determined.

The Ameren Companies discuss the cost and time involved in conducting the CWC analyses. (Ameren IB, p. 29) This argument is misplaced because all of the arguments detailed for the time involved are related to the lead-lag study rather than the methodology applied to the results of the lead-lag study. (Ameren IB, pp. 29 – 30) However, as Staff has previously discussed, the same lead/lag study with few modifications was used by both the Companies and Staff. The net lag and gross lag methodologies differ only in the manner in which the results of the lead-lag study are applied, not in the conduct of the underlying studies. (Staff IB, pp. 31-32)

Further, the Companies' comparison of the revenue lag with the dollar weighted expense lead (Ameren IB, p. 31) is also misleading. If the total annual cash revenues equaled the total annual cash expense, then the difference in the revenue lag days and expense lead days would be meaningful. However, total annual cash revenues do not equal total annual cash expenses and to compare only the revenue lag with the dollar weighted expense lead confuses the issue.

The Ameren Companies argue that Ms. Ebrey reaches an illogical conclusion because her CWC calculation produces a negative CWC allowance while at the same time showing that expenses exceed revenues. Ironically, rather than discrediting Ms. Ebrey's approach, the Companies' argument actually highlights the flaw in their own approach. The flaw is that the Ameren Companies' CWC calculations ignore the difference between the overall levels of operating cash inflows and outflows.

A CWC calculation should consider both the <u>amounts</u> of cash revenues and cash expenses and the <u>timing</u> of when cash is received or paid. To maintain an appropriate balance of cash on hand, one must pay attention to both the amount and timing of cash flows. The Ameren Companies' approach gives insufficient weight to amounts and tips the scale too far in the direction of timing. Then, when criticizing Ms. Ebrey's calculation, the Ameren Companies flip their position and give insufficient weight to timing and tip the scale too far in the direction of amounts. Staff's approach, on the other hand, achieves the appropriate balance between amounts and timing.

Since the Companies' approach gives insufficient weight to amounts, their Net Lag Approach assumes that cash revenues and cash expenses are equal and thus ignores the difference between the overall levels of operating cash inflows and outflows. (*See* Ameren IB p. 31; AmerenCILCO Exhibit No. 6.5; AmerenCIPS Exhibit No. 6.5; AmerenIP Exhibit No. 6.5; Respondents' Exhibits 16.1, 16.2 Revised, 16.3 Revised, 36.1, 36.2, 36.3) As a result, insufficient weight is given to the amount of cash revenues.

When criticizing Staff's approach, Ameren points to Column (C) of Ms. Ebrey's Schedules 13.1, which incorporates amounts, and conveniently ignores columns (D) through (F), which incorporate timing. (*See* ICC Staff Exhibit 13.0 (Corrected), Schedules 13.1 (CIL, (CIPS), and (IPC)) In contrast to the Ameren Companies' approach, Staff's approach is balanced. Staff agrees that if all the weight is pulled off one side of the scales, the scales will no longer be level. However, Staff believes the remedy is to restore the proper weight to each side rather than conclude the scales are broken and replace them with ones that will achieve a desired result. The Commission should accept Staff's CWC adjustments, which reflect the proper balance between amount and timing.

Ameren accuses Staff witness Ebrey of "flip-flopping" regarding which CWC methodology is appropriate. Once again, in their usual fashion, the Ameren Companies have it exactly backwards. The facts are these. Until this current proceeding, the Ameren Companies have been consistent in the CWC method they have proposed to the Commission, namely the Gross Lag Method. In this current proceeding, Staff proposes the Gross Lag Method in calculating CWC. This case is the first time that the

Ameren Companies have proposed the Net Lag Method to the Commission. Thus, it is the Companies that have changed their approach. The Companies are correct that Ms. Ebrey discussed the Net Lag Method in her testimony in Docket Nos. 02-0798, 03-0008, and 03-0009 (Cons.). However, Ms. Ebrey did not use the Net Lag Method, or any method, to derive a CWC requirement for the Ameren Companies in that case. Ms. Ebrey explored using the Net Lag Method as a way of correcting certain deficiencies in the way Ameren proposed to apply the Gross Lag Method in that case, but ultimately recommended that the Commission not grant Ameren a CWC in that case because it had not made sufficient information available to appropriately determine a CWC requirement. (Ebrey Reb., ICC Staff Exhibit 13.0, p. 6)

The Companies' comparison of Accounts Payable and Accounts Receivable (Ameren IB, pp. 31-32) is without merit. Without the details of what is included in either the accounts payable or accounts receivable balances, this comparison is meaningless. For example, Account 142 includes "amounts due from customers for utility service, and **for merchandising, jobbing and contract work** (Uniform System of Accounts for Electric Utilities (emphasis added)), clearly more inclusive than revenues from base rates. Likewise Account 232 includes "all amounts payable by the utility within one year, which are not provided for in other accounts". (*Id.*) Thus, cash expenses such as Taxes accrued (Account 236), Interest Accrued (Account 237), and Tax Collections payable (Account 241) are not considered in the Accounts Payable used by the Companies in its comparison.

Staff's use of the Gross Lag methodology which clearly compares the cash provided by ratepayers through base rates with the day-to-day cash needs of each Company should therefore be approved.

2. Interest Expense Lead

The Ameren Companies claim that Staff is misstating the approach used by the Companies and is being inconsistent in its approach to the interest expense lead. (Ameren IB, p. 32) In its Initial Brief, Staff clearly explained its approach in deriving the appropriate lead days for interest expense based on the number of days in the test year during which the interest expense was incurred. (Staff IB, p. 34) Staff's use of a 91.5 day lead is consistent with the fact that the test year is a leap year. The Companies in their calculation of the CWC requirement also recognize that the test year is a leap year by using 366 days as the denominator to derive the CWC factor they apply to each expense amount. (Adams Sur., Respondents' Exhibit 37.0, p. 47) If the test year is to be recognized as a leap year, then it should be done consistently.

In addition, the total interest expense for Ameren IP has been categorized as it relates to conventional debt reflecting the 91.5 day lead and Transitional Funding Trust Notes ("TFTNs") with a 2 day lead. (Staff IB, Appendix A, Schedule 9 (IPC)) The Companies do not make this distinction in their interest expense CWC calculation for AmerenIP.

3. Capitalized Payroll in CWC Requirements

The Ameren Companies argue that the capitalized portion of payroll would already be included in rate base and as such would already earn a return. (Ameren IB, p. 34) Yet Ameren witness Adams has already agreed that the payrolls paid during the time new rates would be in effect are not reflected in the revenue requirement rate base. (Tr., pp. 531-533) Thus, the cash working capital necessary to cover payroll after rates go into effect could not include any costs already included in rate base. (Staff IB, pp. 34-35) Staff's proposal which accurately reflects the cash needs of the Companies with respect to payroll costs should therefore be approved rather than the Ameren Companies' proposal which only considers payroll costs to the extent they are recorded as expenses of the Companies.

4. Expense levels to which cash working capital factors are applied.

The Ameren Companies did not support or adequately explain the source of the amounts they used to derive each Company's CWC allowance. Staff's CWC calculations are based on the levels of costs included in Staff's rebuttal revenue requirement and other source documents provided by the Companies as referenced on ICC Staff Exhibit 13.0 (Corrected), Schedules 13.01 (CIL), (CIPS), and (IPC). (Ebrey Reb., ICC Staff Exhibit 13.0 (Corrected), p. 16)

As clearly set forth in Staff's Initial Brief, Ameren witness Stafford was unable to reconcile his cost amounts using the information the Ameren Companies provided to Staff. However, he was able to reconcile the cost amounts used by Staff using the information the Ameren Companies provided to Staff. (Tr., pp. 406-457; Staff IB, pp. 35-38) The Ameren Companies failed to address this issue in their Initial Brief. Ameren's Initial Brief under this heading references Section I.F.1. (Ameren IB, p. 35) Under the Table of Contents, the referenced section discusses Unfunded OPEB related to the OPEB Liability and in no way addresses Staff's concerns with the various expense levels and the lack of explanation provided by the Companies for the levels used in their CWC schedules. Clearly, Staff's cost levels should be approved in the derivation of CWC requirements for each of the Ameren Companies. (Staff IB, pp. 35 – 38)

H. Other

II. OPERATING EXPENSES AND REVENUES

A. Summary of Uncontested/Settled Issues

B. Vegetation Management/Tree Trimming

The Ameren Companies contend that the evidence supports rejection of Staff's no-contact interpretation of NESC Rule 218 as adopted under Part 305. (*See* Ameren IB, p. 38) Staff disagrees. As explained in Staff's Initial Brief, the record evidence, the language of NESC Rule 218 as adopted under Part 305 and principles of statutory construction all support Staff's interpretation of NESC Rule 218, (Staff IB, pp. 41-46) Staff also submits that a "no-contact" interpretation of Rule 218 is in the best interests of the citizens of Illinois. Staff witness Mr. Spencer testified that trimming consistent with a no-contact interpretation of NESC Rule 218 is likely to produce real benefits in terms of reducing the likelihood of serious injury or death from citizens coming into contact with utility electric lines in or near trees:

> Based on the above information, the twenty-year average is that nearly 1 death occurs each year and 3 additional injuries occur each year in Illinois in connection with utility electric lines in or near trees. Even though these occurrences could be characterized as "relatively few" or "very rare", each one is important and it is worthwhile, in my opinion, to attempt to minimize these occurrences. While an effective utility tree trimming program which provides better clearances and better visibility of the utility's energized conductors cannot be expected to prevent all of these accidents from occurring, I believe it is likely to reduce the number of such occurrences.

(Spencer Reb., ICC Staff Exhibit 21.0, p. 14) Staff cannot discount the importance of reducing such incidents as Ameren seems to do.

Staff also submits that with more effective tree trimming (i.e., trimming consistent with a no-contact approach), the Ameren Companies can ensure more reliable electric service by reducing damage to its facilities, reducing the number of outages, and reducing the length of outages. The significance of this connection is highlighted by the outages in the Ameren Companies' service territories associated with the large storms that occurred in July of this year. These storms interrupted electric service to upward of several hundred thousand Ameren customers in Illinois with some interruptions lasting several days, and hit home by impacting at least one of the participants in the hearings for these dockets. (Tr., pp. 143-144) While there is nothing a utility can do to prevent all interruptions resulting from severe weather, better tree trimming in the years before a storm can reduce the number of interruptions to some degree and shorten the service restoration process. The Ameren Companies' arguments regarding tree trimming ignore the real world impact of tree trimming on safety and reliability, and must be rejected. Staff also responds to additional arguments made by the Ameren Companies in Section V.C, below.

The Ameren Companies also contend that a no-contact interpretation of NESC Rule 218 as adopted in Part 305 would essentially double tree trimming costs because they would switch from a four-year to a two-year trimming cycle. (Ameren IB, pp. 38-39) Staff has already identified the deficiencies in the Ameren Companies' position regarding additional costs, including their inadequately supported assumption that they would need to switch to a two-year trimming cycle. (*See* Staff IB, pp. 46-51) The

Ameren Companies add nothing new in their Initial Brief, and their arguments should be rejected for the reasons indicated in Staff's Initial Brief. Nevertheless, Staff would like to highlight some of the deficiencies in the Ameren Companies' argument.

The Ameren Companies' criticize Staff witness Mr. Spencer for allegedly not taking issue with the dollar amounts estimated for going to a two-year trimming cycle and for not making any detailed dollar calculations of his own. (Ameren IB, p. 39) The Ameren Companies' first point totally misses the mark, as Staff was not taking issue with the estimate of what it would cost to trim every two years. Rather, Staff's point was that the assumption that the Ameren Companies would need to switch to a two-year cycle is unreasonable. The Ameren Companies also have the unquestioned burden of proof, and their failure to establish the reasonableness of their additional cost estimate does not require Staff or any other party to provide alternative reasonable cost evidence.

Further, the record contains clear evidence refuting and demonstrating the internal inconsistency of the Ameren Companies' additional cost position:

> Based on these numbers, Ameren is predicting that trimming to a "no contact" policy will increase its total annual trimming costs by more than 97%, nearly doubling its present annual trimming costs. At lines 268-269 in Respondents' Exhibit 25.0, witness Wiesehan also states "Our cost estimates for maintaining a no touch program are based upon trimming our entire system at a minimum every two years vs. every four years…". At lines 165- 168 in Respondents' Exhibit 26.0, however, Mr. Clapp describes the current Ameren vegetation management program as one of "combining (a) a 4-year normal pruning cycle with (b) identifying and scheduling any faster growing trees or trees with pruning limitations such that they might become cycle busters for interim inspection or pruning…".
>
> Based on my observations of the state of tree trimming in the service territories of the Ameren Companies in Illinois, the Ameren Companies have some work to do to meet a "no contact" policy, but I believe they are already most of the way there with their combined 4-year and mid-cycle "cycle busters" program. I believe the scope of the additional required

> work is small. If there are significant incremental costs at all, I believe those costs would not come anywhere near doubling the present costs as suggested by Respondents' Exhibit 16.5. In fact, I believe there would be some offsetting O&M cost savings to any incremental increased costs. ….

(Spencer Reb., ICC Staff Exhibit 21.0, pp. 18-19)

While it is clear to Staff that Ameren has work to do to meet a "no contact" trimming policy, it is also clear that the magnitude of the trimming deficiencies Staff has observed in the field would not justify anywhere near the program cost doubling that Ameren wants the Commission to believe. Also, Ameren claims to do mid-cycle "cycle buster" trimming already, as its witness Mr. Clapp has testified. Either Ameren is not already doing the mid-cycle "cycle-buster" trimming as it claims, or its double-the-cost numbers are fiction.

Similarly, the Ameren Companies' response to Mr. Spencer's opinion regarding probable offsetting cost savings from a no-contact policy ignores its burden of proof. (*See* Ameren IB, pp. 42-43) It is incumbent upon the Ameren Companies to provide a reasonable estimate of its claimed additional costs. Staff has provided testimony that better tree trimming practices will reduce damage to facilities and outages that would have otherwise occurred. Specifically, Mr. Spencer opined that there will be some savings of O&M costs because of fewer callouts of Ameren linemen to respond to power interruptions and less damage to Ameren's facilities if the trees are trimmed better. (Spencer Reb., ICC Staff Exhibit 21.0, p.17) The Ameren Companies do not dispute that their cost estimate contains no allowance of any kind for these savings. This evidence establishes the unreasonableness of the Ameren Companies' cost estimate, and the Ameren Companies' attempt to somehow place the burden of proof on Staff and other parties does nothing to remedy this defect.[2]

C. Injuries and Damages Expense

Both Staff and the AG proposed adjustments to AmerenCILCO and AmerenCIPS injuries and damages expense. In rebuttal testimony, the Ameren Companies accepted Staff's adjustments on the basis that the adjustments weight payments against accrued expense and eliminate what Staff considers to be outlying data. (Stafford Reb., Ameren Ex. 16.0, p. 8)

The AG's adjustment for AmerenCILCO and AmerenCIPS is based on a five-year average of actual cash payments charged against the reserve. (Effron Dir., AmerenCILCO AG Exhibit 1.0, p. 18 and AmerenCIPS AG Exhibit 1.0, pp. 15-16) The methodology employed by the AG is a reasonable alternative to Staff's methodology. The fact that the Companies have accepted Staff's adjustments should not preclude the Commission from considering the AG's adjustments.

D. Rate Case Expense

1. Delivery Services

While Staff agrees that its disallowance of rate case expense is not based on any quantitative or qualitative analysis of the Ameren Companies' expenses or rate case estimates, the absence of such an analysis directly results from the Companies' inability or unwillingness to provide Staff with any information with which to conduct such an analysis. It is not clear to Staff how an analysis of an estimate can be performed based

[2] Staff does not separately respond to the arguments contained at pages 43 through 48 of the Ameren Companies' Initial Brief, since that text appears to be an inadvertent duplication of the text and arguments contained at pages 38 to 43 of the Ameren Companies' Initial Brief.

only on a verbal communication, an internal e-mail, or a "lengthy track record." Staff realizes that rate case expense is ongoing and that it is not possible to review all invoices for rate case expense by the time rebuttal testimony is filed, which is Staff's last opportunity to address the issue. Therefore, the preferred procedure is to determine the reasonableness of rate case expense estimates by looking at the bases for the estimates; e.g., reviewing the reasonableness of the service provider hours and hourly rates used to derive an estimate. (Tr., p. 606)

Company witness Stafford testified in surrebuttal testimony that service provider rates, contracts, letters of engagement, and historical data were used to derive rate case cost estimates. (Stafford Sur., Respondents' Exhibit 36.0, p. 11) Of those types of information, only three contracts, one of which related to the BGS proceedings (Docket Nos. 05-0160/05-0161/05-0162 (Cons.)), were provided to Staff in response to requests for how the Companies' estimates were determined. (Jones Reb., ICC Staff Exhibit 14.0, pp. 4-5) At the evidentiary hearings in this proceeding, Mr. Stafford acknowledged that several of the estimates with outside providers were based on verbal communications and that no calculations were performed for other categories of rate case estimates. (Tr., pp. 477-487) Regarding the estimate for outside legal expense (ICC Staff Cross Exhibit 13), Mr. Stafford quibbles that it is not based on verbal communication since he relied on an internal e-mail from Ameren's legal counsel that quantified the estimate. (Tr., p. 486; ICC Staff Cross Exhibit 13)

Staff prefers to rely on vendor invoices only to verify that a company is on track to incur a rate case expense estimate that has been determined to be reasonable. (Tr., p. 590) Because the Ameren Companies were unable or unwilling to provide Staff with any information with which to determine if the rate case estimates were reasonable, Staff had to rely on vendor invoices to verify what percent of a respective estimate had been incurred and should be recovered through rates. (Jones Reb., ICC Staff Exhibit 14.0, p. 5; ICC Staff Exhibit 14.0, Schedule 14.01 (CIL), (CIPS), (IPC))

Staff disallowed the invoices from CSS Consulting and Manpower, Inc. because there was nothing on the invoices to indicate that the services provided were for the rate case proceedings. (*Id.*) This was verified by Ameren witness Stafford, who also could not tell from the invoices that the work performed was for the rate case proceedings. (Tr., pp. 488-489)

Like Ameren, Staff has no crystal ball when it comes to rate case estimates. (Ameren IB, p. 55) Staff does not know how the costs as evidenced by a vendor's invoices relate to Ameren's total estimate for that vendor. So, while invoices can be used to verify that costs have been incurred through a certain date, they do not necessarily support that the total estimated amounts the Ameren Companies want to recover from ratepayers are reasonable. (Jones Reb., ICC Staff Exhibit 14.0, p. 4) It is the Ameren Companies' responsibility to provide sufficient information about how they derived their estimates so that other parties can evaluate the reasonableness of the Ameren Companies' assumptions and how they arrived at the proposed amounts based upon those assumptions. The Ameren Companies simply failed to do so.

Staff's adjustment should be adopted by the Commission because the Ameren Companies should be allowed to recover from ratepayers only those costs that they have adequately and properly supported.

2. Post-2006 Basic Generation Services

Staff's recommendation to allow recovery of procurement proceeding costs through the Supply Procurement Adjustment ("SPA") rather than through delivery service rates is not inconsistent with cost-causation principles, as the Ameren Companies claim. (Ameren IB, p. 58) Said costs were incurred to support the generation procurement proceedings, Docket Nos. 05-0160, 05-0161, and 05-0162 (Consolidated); they are not related to delivery services. (Jones Dir., ICC Staff Exhibit 3.0, p. 5)

Because the costs are related to the proceeding that established how the Ameren Companies will acquire power supply beginning in January 2007, they can reasonably be characterized as power supply costs. (Jones Reb., ICC Staff Exhibit 14.0, p. 11) Power supply costs should be recovered from the customers who purchase their power from the Ameren Companies. Requiring all delivery service customers to pay for the Ameren Companies' power supply costs by allowing recovery of the BGS costs in the instant proceedings imposes costs based on eligibility, rather than on the traditional ratemaking tenet of cost causation. (Jones Reb., ICC Staff Exhibit 14.0, pp. 11-12)

Staff's recommendation is consistent with the Commission's recent decision on this same issue in Docket No. 05-0597:

> At issue is whether or not ComEd should be allowed to recover the costs associated with the procurement case through its delivery service rates. ComEd argues that it should be allowed to recover the costs incurred as a result of the procurement case through delivery service rates as those costs are ultimately a benefit to all customers. Staff opposes ComEd's proposal and in the alternative proposes that ComEd only be allowed to recover its unamortized balance of its procurement case expenses through the SAC. Staff's proposal assigns the cost of the procurement proceeding to those customers who benefit from the procurement process

> rather than to all customers including those who do not take supply from ComEd and those whose electric supply service has been declared competitive. The Commission agrees with Staff that ComEd's proposal to amortize its estimated legal fees and expenses related to the procurement proceedings should be rejected since the costs are not related to delivery services. The Commission finds Staff's proposal more closely aligns with cost causation principles. For this reason, the Commission deems Staff's proposed recovery methodology reasonable and it is hereby adopted. The reduction to procurement expense referenced in the preceding conclusion, which was derived from Staff Exhibit 12.11, page 2 of 2, lines 5-10, will reduce the amount of the procurement expense ComEd will be allowed to collect through the Supply Administration Charge.

(*Commonwealth Edison Co.*, Docket 05-0597, Final Order, July 26, 2006, p. 50, corrected August 1, 2006)

For the same reasons discussed above regarding delivery services rate case expenses (see discussion in Section II.D.1 of this Reply Brief), the Ameren Companies should be allowed to recover through the SPA only those procurement proceeding costs that have been substantiated. (Jones Dir., ICC Staff Exhibit 3.0, p. 7)

For the reasons set forth above, the Commission should accept Staff's proposed adjustments to remove procurement proceedings costs from rate case expense recovered in delivery service rates. Furthermore, the Commission should only allow recovery through the SPA of those procurement proceeding costs that have been substantiated.

3. Depreciation Study

The Ameren Companies argue that the depreciation study was an important and necessary expenditure to determine appropriate depreciation rates for all of the Ameren Companies (Stafford Sur., Respondents' Exhibit 36.0, p. 14), but there is no indication that the study was a necessary part of the instant proceedings. The study supports a change in depreciation rates, yet the Companies requested no change in their rates.

(*Id*., p. 15) The Companies have the temerity to point out that Staff did not request a change in depreciation rates, either (Ameren IB, p. 61); however, it is not Staff's responsibility to make reasonable use of the depreciation study commissioned by the Companies.

The only change requested by the Ameren Companies is permission to reallocate AmerenIP's depreciation reserve, which Staff has recommended that the Commission deny because reallocation does nothing to correct depreciation rates and Staff found nothing to indicate that reallocation of the depreciation reserve is acceptable under the rules of GAAP. (Jones Reb., ICC Staff Exhibit 14.0, pp. 8-9) (see also Section I.E. of Staff IB and this Reply Brief) Staff believes that the reallocation, which has no effect on the current proceedings, is simply a way to make it appear that the Ameren Companies are making some use of the depreciation study in response to Staff's proposed adjustment.

By way of the depreciation study, Ameren became aware of the extent to which its depreciation rates were inaccurate, but it has done nothing to correct those rates. If the difference between actual accumulated depreciation by account/function as reflected in Ameren's general ledger and calculated accumulated depreciation by account/function as determined by the depreciation study is of a magnitude to warrant an adjustment, Ameren should have used the information to correct the problem. Ratepayers should not have to foot the bill for a management tool that has had no impact on the instant proceedings. (*Id*., p. 10)

The Commission should adopt Staff's adjustment to disallow recovery of the cost of the depreciation study because the Ameren Companies have not made reasonable use of the results of the study and should not be allowed to recover the cost from ratepayers.

E. A&G Expenses

1. Functionalization

In their brief, the Ameren Companies defend their proposed levels of A&G expenses and criticize the adjustments proposed by Staff and the IIEC. Nevertheless, their arguments are deficient and fail to undermine in any way the reasonableness of Staff's proposed adjustment of A&G expenses.

The Companies criticize Staff for taking a "generalized view" of A&G, rather than conducting "a review of specific A&G expenses". (Ameren IB, p. 60) The Ameren Companies go on to criticize Staff and the IIEC for not using the "hundreds of Company responses to data requests that deal with A&G expenses" to recommend that specific A&G expenses "be allowed for recovery, or not allowed for recovery". (*Id.*, p. 61) The Ameren Companies go on to complain as follows about the Staff and IIEC adjustments:

> While they allege that a portion of A&G costs support non-regulated production functions, they provide no factual basis for that allegation. Neither witness has identified any specific A&G expenses that do in fact support or relate to non-regulated production functions. They merely assume this to be the case and challenge the Companies to prove them wrong.

(*Id.*) The Companies seek to turn the tables on Staff and the IIEC by arguing that they have failed to support their proposed adjustments to proposed A&G expenses. This argument fundamentally distorts Staff's position on the issue. Staff had criticized the Companies for reallocating costs associated with Ameren Services Company ("AMS") among Ameren subsidiaries according to principles that conflict with Commission decisions in the last round of delivery service cases for both AmerenCIPS and

AmerenCILCO. (Lazare Dir., ICC Staff Exhibit 6.0, p. 21) Furthermore, as Staff has pointed out, the Ameren Companies offer no explanation or justification in their filing for this reallocation of A&G expenses to distribution. (*Id***.,** p. 23)

Despite their own deficiencies on this matter, the Companies lash out at Staff and the IIEC for failing to support their proposed functionalization of AMS-related A&G expenses. Their criticisms are completely unjustified. Staff's proposed allocation of AMS costs is consistent with the method adopted by the Commission in the last round of delivery services cases. (*Id***.,** p. 25) In contrast, the Companies propose an alternative allocation of these expenses that shifts costs from unregulated generation subsidiaries to regulated Companies. Furthermore, the Companies fail to explain the reasons for this alternative allocation. Under these circumstances, the burden clearly lies with the Companies to explain the basis for their alternative approach. However, they have failed to do so and their criticisms of Staff and the IIEC cannot hide this failure. The Companies' arguments should clearly be rejected.

The Companies go on to defend their proposed functionalization of A&G expenses by arguing that the regulated Ameren companies are separate entities from the unregulated companies. According to the Companies:

> none of the [ ] test year A&G expenses support non-regulated production functions of other Ameren affiliates involved in the generation of electricity, because A&G expenses supporting non-regulated production functions of other Ameren affiliates are recorded on the books of the other Ameren affiliates.

(Ameren IB, pp. 61-62) By this statement Ameren is according to itself the right to determine by itself how A&G expenses should be allocated between regulated and unregulated affiliates. In previous proceedings the functionalization of A&G expenses has been a contested issue. Furthermore, in the past the Commission has rejected the methodology adopted by the Ameren Companies to functionalize these expenses. (Lazare Dir., ICC Staff Exhibit 6.0, p. 23) Thus, it is clearly inappropriate for the Ameren Companies in this case to arbitrarily functionalize AMS-related expenses to distribution without explanation.

The Ameren Companies go on to criticize Staff for failing to propose an increase in A&G expenses for AmerenIP when the Companies' proposed revisions to Staff's adjustment produced a higher level of A&G expenses than originally proposed. The Companies complain that Staff is being inconsistent because it proposed upward adjustments in G&I plant for AmerenCILCO but declines to propose an increase in A&G expenses for AmerenIP. (Ameren IB, p. 63)

This criticism has no merit. The two situations are fundamentally different. With respect to AmerenCILCO G&I plant, the Company proposed a level of 2000 test year plant that was below the level approved by the Commission in its previous delivery service case. Staff found no basis to adopt in this proceeding a level of 2000 test year G&I plant that deviates from the Commission approved level in the previous case. There is no similar compelling reason or evidence to indicate that A&G expenses for AmerenIP should be increased in this proceeding over and above the level proposed by the Companies. (Lazare Reb., ICC Staff Exhibit 17.0, pp. 16-17) Therefore, Staff does not propose any increase in A&G expenses for AmerenIP.

2. Incentive Compensation

The costs related to incentive compensation plans should be disallowed because (1) the plans are dependent upon financial goals of the Ameren Companies that primarily benefit shareholders; (2) ratepayers would provide funding even when no costs were incurred by the Companies because the plans' goals were not met; and (3) the plans are discretionary and may be discontinued at any time. Prior Commission practice supports the disallowance of incentive compensation on these grounds. (Jones Dir., ICC Staff Exhibit 3.0, p. 16)

The Ameren Companies choose to misconstrue Staff witness Jones' testimony that, "the plans are dependent upon financial goals of the Companies that primarily benefit shareholders." (Ameren IB, pp. 66 and 70) However, simple sentence construction indicates that the phrase "primarily benefit shareholders" refers to financial goals and not to incentive compensation plans ("ICP"), as the Companies suggest. In light of the fact that the Companies have chosen to incorrectly interpret Staff's testimony (Tr., p. 806), no weight should be given to the Companies' argument that Staff's testimony supports at least a partial recovery of incentive compensation costs because it implicitly acknowledges that ratepayers benefit from the plans. (Ameren IB, p. 70)

Regardless of how the Ameren Companies choose to interpret Staff's testimony, the fact remains that their plans are ultimately dependent upon financial goals of the Companies that primarily benefit shareholders. (Jones Dir., ICC Staff Exhibit 3.0, p. 16) Ameren witness Bauer admits that Ameren must achieve certain levels of financial success, as measured by earnings-per-share ("EPS"), to have money available to fund the ICP. (Bauer Reb., Respondents' Exhibit 23.0, p. 3)

With respect to ratemaking, financial performance goals are based upon circular reasoning; that is, the larger the rate increase granted, the more success Ameren will have in achieving its earnings goals, which will enhance its ability to award incentive compensation. Financial performance goals primarily benefit shareholders; therefore, shareholders should bear the cost of paying incentive compensation. (Jones Dir., ICC Staff Exhibit 3.0, p. 17)

The litany of benefits ascribed to the Ameren Companies' incentive compensation plans (Ameren IB, pp. 66-68) fails to persuade that the plans can reasonably be expected to provide net benefits to ratepayers, a condition that the Commission has stated must be met in order to recover for the plans. (*Illinois Power Company*, ICC Docket No. 01-0432, Order, March 28, 2002, p. 42)

Staff's adjustments to disallow labor and the associated payroll tax expenses related to incentive compensation plans are just and reasonable and should be adopted by the Commission.

3. Pension and OPEB Expense

4. Major Medical

5. Other A&G

F. Effect of Ameren Ownership on Illinois Power Expenses

G. Other

III. RATE OF RETURN

A. Summary of Uncontested/Settled Issues

B. Capital Structure

1. Capital Structure Measurement Period

a. Capital Measurement Period for AmerenCILCO and AmerenCIPS

The Ameren Companies claim that Staff's proposal to measure AmerenCILCO's and AmerenCIPS' long-term capital as of June 30, 2005 while using a 12-month measurement period centered on that date for short-term debt mismatches the measurement periods of long-term and short-term capital. (Ameren IB, p. 75)

As fully explained in Staff's initial brief, the Ameren Companies' arguments are erroneous and should be rejected. (Staff IB, pp. 78-79) There is no rule requiring the end of the measurement period for short-term debt be aligned with the measurement date for long-term capital. In fact, Staff demonstrated that the use of a twelve-month short-term debt measurement period with a midpoint that coincides with the measurement date of the long-term capital structure components, as Staff proposes, better aligns the average balance of short-term debt with the long-term capital structure components.

Further, the Commission should be wary about accepting the Ameren Companies' proposal to switch to a December 31, 2005 capital structure in mid-case due to the multitude of errors Staff found in their original, December 31, 2004 capital structures. Even after the Ameren Companies filed supplemental direct testimony to correct errors in their original proposed capital structures, Staff still found a large number of errors. (*See* Pregozen Dir., ICC Staff Exhibit 5.0, lines 122-134, 309-311, 324-334, 339-340, 455-459, 498-503, and 518-525) Staff has also found errors in the December 31, 2005 capital structures. For example, AmerenCILCO preferred stock schedule presented in the Ameren Companies' surrebuttal testimony (Ameren Exhibit 35.1, p. 1) reflects no annualized amortization of either the issuance expense for the $4.64 series or the losses on the reacquired issues, despite recording unamortized balances for those accounts. Additionally, the unamortized losses on reacquired issues in Ameren Exhibit 35.1 are the same as those presented in Staff Ex. 16.0, Schedule 16.04 (*i.e.*, the Ameren Companies' preferred stock schedule fails to reflect the six months of amortization from June 30, 2005 to December 31, 2005). Further, for AmerenCIPS, the December 31, 2005 unamortized balance of debt expense for Pollution Control Series 2004 is only $32 million lower than the December 31, 2004 balance, although the annual amortization of debt expenses is listed as $54 million.[3] (Respondents' Exhibit 15.3 and AmerenCIPS Exhibit 5.2) All these documented errors indicate the Ameren Companies' estimates of their costs of capital are unreliable.

b. Capital Measurement Period for AmerenIP

The Ameren Companies recommend measuring AmerenIP's long-term capital as of December 31, 2005 with a 12-month measurement period ending on that date for short-term debt. The Ameren Companies suggest that their proposal is necessary to provide consistency with the measurement periods used for AmerenCILCO and AmerenCIPS and to incorporate final purchase accounting adjustments related to the acquisition of AmerenIP.[4] The Ameren Companies further claim that there needs to be a compelling reason to use a different measurement date for any of the three Ameren Companies. (Ameren IB, pp. 76 and 87-88)

The Ameren Companies' arguments are baseless and should be rejected. In fact, if any party needs to provide a compelling reason for its position, it is the Ameren Companies, who proposed to switch AmerenIP's measurement date in the middle of the

[3] This list is a sample of the errors Staff found. It is not complete.

[4] Under purchase accounting, AmerenIP's assets and liabilities were restated to reflect their fair market value rather than their original depreciated book value. Any such adjustments made <u>prior</u> to the capital structure measurement date would have to be excluded from the rate making capital structure.

proceeding. As fully explained in Staff's initial brief, AmerenIP does not need to have the same measurement date as the other two Ameren Companies. (Staff IB, pp. 79-81) Moreover, removal of purchase accounting adjustments that occurred after December 31, 2004 is necessary only if a capital structure measurement date is adopted that is after December 31, 2004. Thus, there is no need to deviate from the December 31, 2004 capital structure measurement date the Ameren Companies and Staff originally proposed. In fact, such a change in direction is not only unnecessary, but would be inappropriate for two reasons. First, centering the short-term debt measurement period on the long-term capital measurement date, which better aligns the average balance of short-term debt with the long-term capital structure components, was not possible with a December 31, 2005 measurement date. Second, Staff cannot support the accuracy of the proposed purchase accounting adjustment, given the abbreviated time allotted for review during the rebuttal phase of the proceeding and the number of mistakes in the Ameren Companies' previous filings in this docket. For example, in addition to the mistakes noted above, the December 31, 2005 balance of TFTNs for AmerenIP presented in Respondents' Exhibit 15.6 does not match the December 31, 2005 balance of TFTNs shown in AmerenIP Ex. 5.4, p. 1. Thus, the December 31, 2004 capital structure measurement date the Ameren Companies and Staff originally proposed for AmerenIP's long-term capital should be adopted, with a 12-month measurement period centered on that date for short-term debt.

c. Retirement of Short-Term Debt in May 2005

The Ameren Companies argue that Staff erred by not adjusting AmerenCILCO's actual January through April, 2005 short-term debt balances to reflect an equity infusion that occurred in May of 2005. (Ameren IB, pp. 83 and 86-87) In addition, the Ameren Companies criticize as "conjecture" Staff's argument that AmerenCILCO's actual short-term debt balances best represent its typical balance of short-term debt. (Ameren IB, p. 75)

The Ameren Companies are wrong, as was fully explained in Staff's Initial Brief. (Staff IB, p. 82) The Ameren Companies' argument is based on faulty logic. Their argument, that the short-term debt balance would be "misleading and overstated" without the adjustment they propose, is only true if one first assumes their desired conclusion (*i.e.*, that the adjustment is proper). The Ameren Companies, however, provided no evidence to support that assumption. They simply speculate that the $100 million reduction of short-term debt, from an equity infusion that occurred in May of 2005, would be "permanent." However, Staff showed that the "permanent" reduction to short-term debt the Ameren Companies cite almost immediately began to be reversed with the issuance of new short-term debt. Thus, AmerenCILCO's actual short-term debt balances better represent AmerenCILCO's typical outstanding balance of short-term debt.

In addition, the Ameren Companies' accusation of conjecture on Staff's part is merely an attempt at defense via offense. Their proposal to deviate from AmerenCILCO's actual short-term debt balances by pretending that a short-term debt refinancing occurred five months earlier than it did, based only on the speculation that the refinanced short-term debt will never be replaced, is absolute conjecture. In fact, the Ameren Companies' argument is not only based on speculation, but on speculation that is highly doubtful, as demonstrated by the immediate replacement of short-term debt noted above. In contrast, Staff used AmerenCILCO's actual short-term debt balances and provided evidence indicating that those balances better represent AmerenCILCO's typical outstanding balance of short-term debt. Thus, the Ameren Companies' arguments should be rejected and Staff's proposal should be adopted.

2. Imputed Capital Structures

CUB argues that the Commission should impute a capital structure to produce financial ratios consistent with a BBB rating and implies that Staff imputed a capital structure based on a BBB target rating in Commonwealth Edison Company's ("ComEd") most recent delivery service rate case (Docket No. 05-0597). (CUB IB, p. 5)

The implication of a parallel between Staff's approach in Docket No. 05-0597 and CUB's approach in the instant docket is erroneous and should be disregarded. First, CUB fails to explain how testimony from a different Staff witness (Ms. Kight as opposed to Mr. Pregozen), in a different docket (Docket No. 05-0597), regarding a different utility (ComEd), has any relationship to the Ameren Companies. Therefore, its argument should be given no evidentiary weight. Indeed, a closer examination of Staff's proposal in Docket No. 05-0597 shows that it has no bearing on the instant case. In the instant docket, CUB is imputing a capital structure, whereas Staff did not impute a capital structure for ComEd. In Docket No. 05-0597, Staff used a capital structure reflecting the proportions of capital actually used to fund ComEd's delivery service rate base (*i.e.*, its <u>actual</u> capital structure). (Pregozen Corr. Reb., ICC Staff Exhibit 16.0, p. 22, n. 31) The <u>actual</u> capital structure was derived by adjusting ComEd's reported capital structure to reflect purchase accounting. Unfortunately, ComEd had proposed an insufficient purchase accounting adjustment to its capital structure; thus, Staff was compelled to make an additional adjustment to correct ComEd's proposed adjustment. (ICC Docket No. 05-0597, Final Order dated July 26, 2006, pp. 115-117) Those corrections enabled Staff to arrive at the true capital structure supporting ComEd's delivery service rate base. (*Id.*) Thus, Staff did not impute a capital structure for ComEd, which is in contrast to CUB's approach in the instant docket.

In addition, contrary to CUB's implication (*see*, CUB IB, p. 5), Staff did not target a BBB credit rating in Docket No. 05-0597. (Pregozen Corr. Reb., ICC Staff Exhibit 16.0, pp. 23-24) Rather, after determining ComEd's actual capital structure, Staff then reviewed the financial ratios resulting from its recommendations to determine whether ComEd's actual capital structure was appropriate for rate setting. Staff concluded that the resulting financial ratios were consistent with those of an A– company and, thus, the actual capital structure Staff calculated was appropriate. (Pregozen Corr. Reb., ICC Staff Exhibit 16.0, lines 442-445; ICC Docket No. 05-0597, Final Order dated July 26, 2006, pp. 117-122)

3. CILCO $4.64 Preferred Stock Expense

The Ameren Companies maintain that the Commission should accept an undocumented issuance expense related to AmerenCILCO's $4.64 preferred stock series because it was embedded in AmerenCILCO's most recent gas and electric rate proceeding Orders. (Ameren IB, pp. 82-83) The Ameren Companies argue that Staff's opposition to the expense lacks substance and is illogical. They argue that if Staff had overlooked an expense adjustment in prior proceedings, that would result in the exclusion of the expense rather than its inclusion.

The Ameren Companies are wrong on all counts; Staff's opposition to the $4.64 series issuance expense is neither lacking in substance nor illogical. To the contrary, the Ameren Companies' arguments are just another weak attempt at defense via offense. Indeed, their arguments sidestep the real issue raised by Staff – that they failed to provide documentation to support their adjustment in this proceeding. (Staff IB, pp. 84-85) First, contrary to the Ameren Companies' claim, an oversight by Staff most certainly could result in the improper inclusion of an expense; the Ameren Companies' failure to see this does not constitute faulty logic on Staff's part. The Ameren Companies' argument implies that Staff builds its estimate of the embedded cost of preferred stock from scratch. That is false. Staff starts with the utility's estimate of the embedded cost of preferred stock and adjusts it, as needed. (*See*, Pregozen Dir., ICC Staff Ex. 5.0, pp. 17-18) Consequently, if a company's initial filing reflected an improper expense and Staff failed to make an adjustment to exclude that expense, it would likely end up improperly included in rates. Thus, Staff's position is not illogical at all.

Second, Staff's opposition is clearly not without substance. In fact, logic dictates that the Ameren Companies' position must be rejected. The inclusion in rates of any expense is improper unless that expense is adequately documented. (220 ILCS 5/10-103 (*stating* that ". . . any finding, decision or order made by the Commission shall be based exclusively on the record for decision in the case . . ."; *see also*, Staff IB at 84-85, addressing this argument in further detail) Since the $4.64 series issuance expense was included in AmerenCILCO's most recent rate Orders, either Staff failed to exclude an undocumented and, thus, improper expense in those proceedings or AmerenCILCO provided adequate documentation of that expense. Contrary to the Ameren Companies' implication, the improper inclusion of an expense based on a Staff oversight in a prior proceeding is a mistake the Commission is not obligated to repeat (*see id.*); in fact, the Commission clearly should not repeat that mistake. Alternatively, if the issuance expense was supported by proper documentation in previous proceedings, then the Ameren Companies should have had no problem producing those documents in the instant docket. The Ameren Companies cannot expect Staff to do what they apparently failed to do – maintain financial records documenting expenses the Ameren Companies incurred and wish to recover. Ultimately, the Ameren Companies are responsible for documenting the expenses they seek to recover. They failed to do so for the $4.64 series issuance expense. Thus, that expense must be excluded in this proceeding regardless of its treatment in prior proceedings.

C. Measurement date of Short-term and Variable Interest Rates

The Ameren Companies claim that recent Staff practice is to update short-term and variable rate interest rates in its rebuttal testimony. The Ameren Companies' sole support for this claim is a citation to an AmerenCIPS and AmerenUE gas rate case (Docket Nos. 02-0798/03-0008/03-0009 (cons.)), in which Staff witness Michael McNally updated his cost of variable rate pollution control bonds in his rebuttal testimony and cited the Commission Order from Docket No. 99-0534, which notes that "the most recent market spot rate" had been adopted in multiple prior cases. (Ameren IB, pp. 83-84)

The citations relied upon in the Ameren Companies' argument are presented out of context to blatantly mischaracterize "recent Staff practice." It is not Staff practice, recent or otherwise, to update its cost estimates throughout a proceeding. First, the reason Staff witness McNally "updated" his position in his rebuttal testimony in Docket Nos. 02-0798/03-0008/03-0009 (cons.) was to change, at the petitioner's insistence, the interest rate source used. (Tr., pp. 1051-1055) The change was not simply to use data from a more recent date, as argued by the Ameren Companies. (*Id.*) The record in Docket Nos. 02-0798/03-0008/03-0009 (cons.) does not indicate that Staff would have made such an "update" if not for that change in source. Furthermore, it is not clear from that record whether Mr. McNally had, at the time of his rebuttal testimony, interest rate data from the new source from the date of his original analysis (i.e., Mr. McNally may have had to use the interest rate from the later date in order to use the new source at all). (Tr., pp. 1068-1070)

Second, the record from Docket No. 99-0534 indicates that Staff's use of "the most recent market spot rate" refers to the rate available at the time of Staff's direct testimony analysis. (Tr., pp. 1055-1060) In contrast, the Ameren Companies' interpretation of that phrase would suggest a continuous updating at every stage of the proceeding. As discussed in Staff's initial brief, to update at every phase of the proceeding is impractical. (Staff IB, p. 86) Moreover, Staff does not endorse updating in later rounds of testimony, unless good cause is shown. Staff does not view updating simply to implement a more recent, higher interest rate to be good cause. (Staff IB, p. 86)

Curiously, the Ameren Companies state that the date Staff adopted for measuring the cost of variable rate and short term debt "conveniently" falls before a period in which interest rates rose. (Ameren IB, p. 85) This is yet another baseless attempt at defense via offense. The Ameren Companies seem to imply that it would be "convenient" for Staff to use a date that produces a lower rate. However, it is unclear how that would be "convenient" for Staff, as Staff has absolutely no stake in the rates the Ameren Companies charge.[5] In contrast, the Ameren Companies very much have a stake in the rates they charge. Coincidentally, Mr. O'Bryan proposed to update to a spot rate as of a date after interest rates had risen. (See, O'Bryan Reb., Respondents' Exhibit 15.1, pp. (page number omitted from exhibit)) This is in contrast to Mr. O'Bryan's proposal in Docket Nos. 02-0798/03-0008/03-0009 (cons.), in which he proposed to use a historical average interest rate.[6] (ICC Docket Nos. 02-0798/03-0008/03-0009 (cons.), Final Order dated October 22, 2003, p. 70) It is "convenient" for the Ameren Companies that in both instances, Mr. O'Bryan's inconsistent proposals produced a higher cost of capital than Staff recommended. This is a prime example of how a company could use selective updating to achieve a higher return, a concern Staff's expressed in its initial brief. (Staff IB, p. 86) Based on the foregoing, the Company's proposal to update its short-term and variable rate interest rates midway through this proceeding should be rejected by the Commission.

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[5] The Ameren Companies' lamentation implies that Staff seeks, for some inexplicable reason, to harm the Ameren Companies. However, the fact that Staff moved its measurement date to April 4, 2006 (to be consistent with that of the other components), which increased the cost of capital, indicates otherwise.

[6] In fact, Staff used the phrase "the most recent market spot rate" to distinguish Staff's recommendation from the historical average interest rate Mr. O'Bryan proposed.

D. Cost of Illinois Power TFTNs

The Ameren Companies continue to argue that Transitional Funding Trust Notes ("TFTNs") are "far different from most bonds," since AmerenIP remits TFTN collections to the trustee on a daily basis. They also claim that Staff's approach improperly assumes that TFTN collections are remitted monthly. (Ameren IB, 88-89)

The Ameren Companies' arguments were fully addressed in Staff's initial brief. (Staff IB, pp. 87-89) Staff explained that the difference the Ameren Companies highlight between TFTNs and regular debt is merely a difference in lead time, which should be, and already is, accounted for through Staff's working capital adjustment. (*Id.*) Thus, to adjust for this lead by adjusting the cost of capital would not only be theoretically incorrect, but would constitute a double adjustment. (*Id.*) Further, since the lead time issue is addressed through working capital, the timing of TFTN remittances is immaterial to the cost of capital. (*Id.*) Thus, Staff's annualization from a monthly periodic rate, which was employed because the TFTN data was presented by the Ameren Companies in monthly terms, makes no assumptions with regard to the timing of TFTN remittances. (Pregozen Corr. Reb., Staff Exhibit 16.0, pp. 11-12: see also, AmerenIP Ex. 5.4, pp. 1-2) Therefore, the Ameren Companies' claim that Staff's approach assumes that TFTN collections are remitted monthly is false and should be rejected. In fact, Staff's proposal reflects the theoretically correct calculation of the interest rate for TFTNs and should be adopted.

E. Cost of Equity

Staff's Initial Brief thoroughly covered the analyses and arguments presented by the various parties' witnesses regarding the cost of equity. (Staff IB, pp. 89-125) Staff will comment further only in response to the Ameren Companies' arguments against the risk adjustment that Staff witness Freetly made to her utility sample's cost of equity to reflect the lower risk of each of the Ameren Companies. (Ameren IB, pp. 112-117)

Staff's Response to Ameren's Initial Brief

The Ameren Companies claim that Staff's downward adjustment to the utility sample's cost of equity is not warranted because Ms. Freetly's ratio analysis implies higher credit ratings than the Ameren Companies currently have and attempts to predict the future credit ratings of AmerenCILCO, AmerenCIPS and AmerenIP. (Ameren IB, pp. 113, 116) The Ameren Companies further argue that Staff improperly uses the S&P published financial ratio guidelines. (Ameren IB, pp. 114-116) Ameren also suggests that Staff's adjustment cannot be empirically justified given the results of the DCF analysis that Ms. McShane presented using all of the sample companies. (Ameren IB, p. 117) Throughout the course of this proceeding, Staff has clarified that the credit ratings implied by its ratio analysis are not a prediction of what the ratings will be or should be and that it used the S&P published financial ratio guidelines in an appropriate manner. (Staff IB, pp. 97-100)

According to the Ameren Companies, the principal problem with Ms. Freetly's analysis is that she allegedly assumes that the Companies will have higher credit ratings than they currently have even though the Companies' credit ratings are actually going down due to factors that are outside the scope of this proceeding and which the final order in this case will not and cannot address. (Ameren IB, p. 113)

As noted in Staff's Initial Brief, Moody's downgraded the ratings of AmerenCILCO and AmerenCIPS on July 26, 2006 to reflect the ". . . difficult political and regulatory environment for electric utilities in the state of Illinois." (Ameren Cross Freetly Exhibit 1 ("Moody's Rating Action")) Moody's Rating Action does not alter the soundness of Ms. Freetly's assessment of the Ameren Companies' cost of equity. Ms. Freetly accounted for the regulatory uncertainty facing the Ameren Companies by using the S&P business profile score of 4 as a measure of the Companies' business risk. (Freetly Corr. Dir., Staff Exhibit 4.0 Corr., p. 4; *see also*, Staff IB, p. 100) To assess the financial risk of the utilities, Staff determined the forward-looking level of financial risk that the utilities will face on a stand-alone basis. The strong funds from operations ratios ("FFO ratios") indicate that the financial strength of the Ameren Companies should improve as a result of Staff's revenue requirement recommendations in this proceeding. (Freetly Reb., Staff Exhibit 15.0 Corr., p. 4) Ms. Freetly accounted for the FFO ratios by translating them into credit ratings, in order to compare the risk level of the delivery service operations of the Ameren Companies to that of her utility sample. Thus Staff's analysis of the Ameren Companies cost of equity is reasonable.

The Ameren Companies incorrectly assert that Staff's implied forward looking credit ratings are a prediction of future credit ratings. (Ameren IB, p. 113, 116) The implied forward looking credit ratings offered by Staff in testimony represent the level of financial strength inherent in Staff's revenue requirement recommendations for the delivery service operations of each company -- AmerenCILCO, AmerenCIPS and AmerenIP. Whereas in contrast, the credit ratings assigned by S&P are based on the consolidated credit profile of the Ameren family of companies. The higher credit ratings indicated by Ms. Freetly's ratio analysis are not meant to imply that the Ameren Companies' actual credit ratings will go up to that level if Staff's position is adopted by the Commission. They simply represent the financial strength of the delivery services portion of the utilities' operations, which Staff then used as a relative gauge of the riskiness of the Ameren Companies in comparison to Staff's utility sample. (Staff IB, p. 100)

In addition, the Ameren Companies mention several reasons why they believe that S&P's published financial ratio guidelines should not be the sole basis for the reasonableness of a recommendation for a given cost of equity, weighted average cost of capital, capital structure (including any hypothetical capital structure) and revenue requirement. (Ameren IB, p. 114) As Staff will show below, none of the reasons they mention invalidate Ms. Freetly's use of the S&P financial ratio guidelines to compare the riskiness of the Companies to her utility sample.

First, Ameren argues that since the ratio guidelines are not definitive in terms of the assignment of a rating, any given rating will not automatically be assigned simply by achieving one or more of the ratio guidelines for a given rating level. (Ameren IB, p. 114-15, (1) in block quote) Ameren also argues that rating agencies are the arbiters of credit ratings. (*Id*., (3) in block quote) Ms. Freetly never suggested that simply because the Ameren Companies' metrics fall within the guideline ranges that the related rating will result. Staff witness Freetly translated the funds from operations interest coverage and funds from operations to total debt ratios (collectively "FFO ratios") that would result from Staff's proposed revenue requirements into implied credit ratings to allow for a straight-forward apples-to-apples comparison of the financial strength of the Ameren Companies to the financial strength of her utility sample. Ms. Freetly never stated that the Ameren Companies would have or attain the implied credit ratings she developed.

In fact, Ms. Freetly used the S&P financial guideline ratios in a manner consistent with Mr. Nickloy's use of those guideline ratios in Docket No. 06-0179[7]. (Staff IB, pp. 98-99)

Second, the Ameren Companies argue that the FFO ratios Ms. Freetly relied on only account for the ratio guidelines of S&P. (Ameren IB, pp. 115-16, (2) in block quote) Although correct, that does not invalidate Ms. Freetly's analysis. Clearly, only S&P financial guidelines are appropriate for translating FFO ratios into implied S&P credit ratings. That is, using S&P financial guidelines to translate FFO ratios into Moody's credit ratings is inappropriate since Moody's might have different guidelines for its credit ratings. Conversely, using Moody's financial guidelines to translate FFO ratios into S&P credit ratings is inappropriate.[8] Since Staff witness Freetly did not use either Moody's (or Fitch) credit ratings to select her sample companies, it would be inappropriate to consider financial ratio guidelines from other rating agencies, even if such financial ratio guidelines were published.

Third, the Ameren Companies' argue that the rating agencies make certain adjustments as part of their ratio analysis to remove the debt and cash flow related to AmerenIP's transitional funding trust notes ("TFTNs") and impute a debt equivalent for purchased power agreements. The Ameren Companies claim that any ratio analysis must reflect such adjustments in the same manner as performed by the rating agencies given the potential magnitude of these adjustments. (Ameren IB, p. 115, (4) in block quote) Although the credit rating agencies exclude TFTNs and the associated interest

[7] Docket No. 06-0179 is a Certificate of Public Convenience & Necessity/Good Standing/Service Authority (8-406,13-403,13-404,13-405,15-401,16-108,16-115,19-110) for the construction and operation of new transmission lines.

[8] The record contains no evidence on the financial guidelines that Moody's uses, if any, in its ratings process.

and principal amortization from their evaluation of a utility's creditworthiness, that approach is not appropriate for assessing a utility's financial strength in the context of an analysis of its cost of common equity. Credit rating agencies attempt to measure default risk. Whether an adjustment should be included in a ratio analysis depends on whether the ratio analysis is used to evaluate cost of common equity or default risk.

In measuring the default risk of AmerenIP's conventional debt, the interest and principal repayment obligations to TFTN holders are removed from AmerenIP's cash flows. Since TFTN holders have first claim to AmerenIP's cash flows, a holder of AmerenIP's conventional debt would be interested in the utility's ability to meet its obligations to conventional debt holders after the obligations to its TFTN holders have been paid. In contrast, the common equity holder's claim to a utility's cash flow is subordinate to both the TFTN holder and the conventional debt holder. Consequently, the relative claim of the TFTN holder and conventional debt holder is of no concern to the common stockholder. Rather, the common stockholder would be more interested in the combined effect of both TFTNs and conventional debt on a utility's cash flow. Thus, when evaluating the cost of common equity, it makes no sense to distinguish TFTNs from conventional debt by removing only TFTNs and their associated cash flows from the computation of financial ratios when assessing financial strength. (Pregozen Corr. Reb., ICC Staff Exhibit 16.0 Corr., pp. 19-20)

Ameren also contends that S&P imputes a debt equivalent for power purchase agreements and since the Ameren Companies will continue to obtain their power supply requirements from third parties, they claim that the purchased power debt imputation issue could remain significant for AmerenIP and become a major issue for AmerenCIPS and AmerenCILCO once new power supply arrangements are entered into for periods post 2006. (Ameren IB, pp. 115-16) Standard & Poor's ("S&P") recently announced it could impute debt to the Companies if recovery is not assured but it does not expect to do so:

> …Typically, Standard & Poor's adjusts the financial statements for purchased power obligations. Since CIPS and CILCO purchase power from affiliates and Illinois Power's purchased power contract with Dynegy Inc. ends on Dec. 31, 2006, Standard & Poor's has not add[ed] a debt equivalent to Ameren's financial statements. <u>Because it appears that an auction process will be established that will enable the companies to pass generation costs through to customers, thereby not exposing them to power providers' performance risk, Standard & Poor's does not expect to assign a debt equivalent to these obligations in the future.</u> However, if recovery is not assured, Standard & Poor's will take the net present value of future annual capacity payments (discounted at the companies' average cost of debt) to arrive at a debt equivalent. Standard & Poor's will add to the balance sheet only a portion of this amount, recognizing that such contractual arrangements are not entirely the equivalent of debt. The percentage that is added is a function of Standard & Poor's qualitative analysis of the specific contracts and the extent to which market, operating, and regulatory risks are borne by the utility.[9]

(Pregozen Corr. Reb., ICC Staff Exhibit 16.0 Corr., pp. 18-19)

Hence, no adjustment will be necessary since the auction process should allow the utilities to recover the costs associated with their prudent purchased power obligations.

Ameren claims that Staff witness Freetly's downward adjustment to her utility sample's cost of equity to reflect the lower risk of the Ameren Companies cannot be empirically justified. (Ameren IB, p. 117) Staff provided the empirical justification for its downward adjustment in its Initial Brief. Ameren calculated the DCF cost of equity for

[9] *Emphasis added,* Standard & Poor's Ratings Direct, "Research: Ameren Corp.", June 14, 2006.

all the companies that were included in the utility samples of the five cost of equity witnesses in this proceeding and showed that the return on equity was actually higher for the less risky companies. As explained in Staff's Initial Brief, Staff's downward adjustments were made to the average of the DCF and risk premium estimates of its utility sample's cost of equity, not the DCF estimates alone. Staff showed that when both the DCF and risk premium methodologies are taken into account, the return on equity is higher for riskier companies with lower credit ratings. The analysis in Staff's Initial Brief confirms the very foundation of financial theory, that investors require higher returns to accept greater risk and, conversely, investors' required rate of return is lower for investments with less exposure to risk. (Staff IB, pp. 97-98)

In conclusion, Staff's development of implied forward looking credit ratings factored in the effect of the capital structure and revenue increases recommended by the Staff on the Ameren Companies' financial strength. Since the FFO ratios for the Ameren Companies imply that AmerenCILCO, AmerenCIPS and AmerenIP are lower in risk than Staff's utility sample, Staff's downward adjustment properly reflects the lower required rate of return that investors would require. The strong FFO ratios show that Staff's recommended cost of equity for each of the Ameren Companies is reasonable and will allow the utilities to maintain their financial integrity and attract capital on reasonable terms. (See Staff IB, pp. 92-94)

F. Other

G. Recommended Rate of Return on Rate Base

As set forth in Staff's Initial Brief, Staff proposes the following rate of return on rate base for each Ameren Company:

Ameren Company	Rate of Return on Rate Base[10]
AmerenCILCO	7.88%
AmerenCIPS	7.95%
AmerenIP	8.26%

The rates of return for each company incorporates the rate of return Staff witness Freetly recommends for common equity.

IV. RATE DESIGN

A. Summary of Uncontested/Settled Issues

1. Rider QF Second Section-QSWEFS

As set forth in Staff's Initial Brief, Staff witness Griffin testified that certain changes were necessary for the Ameren Companies proposed Rider QF, second section, concerning Qualified Sold Waste Energy Facilities ("QSWEF"). (Staff IB, pp. 130-131) The Ameren Companies in their Initial Brief consistent with the rebuttal of Mr. Jones accepted all of Mr. Griffin's proposed changes to the second section of Rider QF. (Ameren IB, p. 118) Given the above, Mr. Griffin's proposed changes to the Ameren Companies' proposed Rider QF second section as set forth in Schedule 11.01 to Mr. Griffin's direct testimony, should be adopted by the Commission.

[10] Pregozen Corr. Reb., ICC Staff Exhibit 16.0, Schedule 16.06.

B. Customer Class Issues

C. Cost of Service Issues

1. Segregation and accounting for delivery service and generation-related uncollectible expenses

2. Development of Meter Costs v. Customer Costs

D. Inter-Class Allocation Issues

1. Allocation methodology

The Illinois Industrial Energy Consumers ("IIEC"), in its initial brief, states that it no longer opposes the Ameren Companies' proposed inter-class revenue allocation[11]. (IIEC IB, p. 41) The IIEC's position is based, in large part, on the Ameren Companies' decision not to increase the DS-4 class revenue allocation in order to partially fund customer class DS-1 rate relief. (*Id*.) The result of this change is that the DS-4 class does not contribute to DS-1 rate relief. (see, Staff IB, pp. 134-139) Customer class DS-4 should be included in any rate relief granted to customer class DS-1 because it is the largest customer class in terms of kWh usage across the combined Ameren Companies' service area and is proposed to pay by far the lowest average amount per kWh of usage compared to the other Ameren customer classes. (*Id*., p. 139)

Though the alternative retail electric supplier ("ARES") market in the Ameren Companies' service areas cannot be considered vibrant, the DS-4 customer class appears to be in the best position, of customer classes DS-1 through DS-4, to take advantage of the ARES market. (Luth Reb., Staff Exhibit 19.0, pp. 5- 7) A customer

[11] Staff notes that IIEC and Staff have addressed the issue of AmerenCILCO's customer class DS-4 revenue allocation, or subsidization, in different sections of their respective initial briefs. Since Staff is responding to IIEC, it is including its response in this section, which is the section that IIEC addressed the argument in its initial brief. For clarity, Staff notes that its initial arguments on this issue are included in Section IV.B., pages 134 through 139, of its initial brief.

would probably not choose an ARES over Ameren supply unless the ARES option offered an economic advantage. (*Id*., p. 7) Over the course of 2005, the most recent complete year of reporting through the Form 21ILCC filed with the Commission by the three Ameren distribution companies, Large and Industrial customers have taken advantage of the ARES market to a far more significant extent than other customer classes, particularly customer class DS-1. (*Id*., p. 6- 7) Month-to-month, the level of kWh sales from ARES to DS-4 customers may fluctuate considerably, but over the course of the most recent year, advantages provided by the ARES market to Large and Industrial customers were far more apparent than the advantages to other customer classes. The 2005 Form 21ILCC sales statistics for the Ameren Companies demonstrate that, during the transition period, when bundled rates were frozen, the potential for economic advantages available to Large and Industrial customers through the ARES market is apparently far more significant than other customer classes. (*Id*., p. 7)

Current bundled rates are subject to increase, not only as a result of this docket but also from possibly higher power supply costs established in the power supply auction. Since customer class DS-1 will absorb the largest average increase per kWh compared to other customer classes under Ameren's proposed rates in this docket and has apparently had no opportunity to offset increased power supply costs through the ARES market, it is reasonable for the Commission to consider rate relief for customer class DS-1. (Staff IB, pp. 136-137) Since DS-4 customers will pay a far lower rate per kWh than other customer classes under the Ameren Companies' proposed rates, because DS-4 customers are the largest customer class in terms of kWh delivered, and because it is apparent that DS-4 customers have far more opportunities to benefit from ARES, the DS-4 customer class is best able to absorb and offset an increase in delivery service rates resulting from rate relief for DS-1 customers. (Luth Reb., ICC Staff Exhibit 19.0, pp. 5-6) Including the DS-4 customer class in the funding of DS-1 rate relief would also have the effect of reducing the increase to the DS-2 and DS-3 customer classes because the increase above cost of service could be spread over a larger revenue and sales base than if the funding for DS-1 rate relief was limited to customer classes DS-2 and DS-3. A reduced increase in the rates of customer classes DS-2 and DS-3 would help resolve the concerns expressed by Staff and Kroger concerning customer classes DS-2 and DS-3. (Staff IB, pp. 141-142; Kroger IB, pp. 4- 5 and 8) Staff supports Kroger's secondary position in which rate relief for customer class DS-1 would be funded by an increase above cost of service not only in the rates of customer classes DS-2 and DS-3, but also the rates of customer class DS-4.

2. Minimum Distribution System Study

E. Rider QF

Staff witness Rockrohr recommended that the Ameren Companies include a fixed-price compensation option, expressed in cents per kilowatt-hour, within Rider QF. (Staff IB, pp. 144-147) Staff is concerned that without such a fixed price option, such as has been offered in each of the Ameren Companies' previous QF tariffs, potential QF customers would find it very difficult if not impossible to conduct a meaningful cost analysis to determine whether to proceed with a QF project, or whether to interconnect existing generation to the utility's system for the purpose of selling excess energy. (Rockrohr Dir., ICC Staff Exhibit 9.0, p.17; Staff IB, p. 145)

The Ameren Companies are opposed to Mr. Rockrohr's recommendation and in one of the arguments made in their initial brief in support of their position, they claim that "Staff witness Rockrohr did not object to the use of locational marginal pricing but recommended the Ameren Companies include a fixed price payment option within Rider QF." (Ameren IB, p. 135) The Ameren Companies have misrepresented Staff's position. A review of Mr. Rockrohr's testimony shows that Staff witness Rockrohr said that he would not object to the use of locational marginal pricing <u>so long as</u> a fixed-price option is also offered. (Rockrohr Dir., ICC Staff Exhibit 9.0, p.18 (emphasis added))

Staff's position that the Ameren Companies should offer a fixed price option was based upon the same concerns which led staff to take the same position in Commonwealth Edison Company's ("ComEd") recent delivery services docket, ICC Docket No. 05-0597. In that docket, ComEd's QF tariff was identified as Rider POG. In ICC Docket 05-0597 the Commission found Staff's recommendation to require ComEd to include a fixed price option within its Rider POG to be just and reasonable. (ICC Docket No. 05-0597, Order entered July 26, 2006, pp. 232-233) The Commission ordered that ComEd's Rider POG be modified to "include Staff's proposal" with "spot prices as an alternative to an expressly stated rate." The Commission further ordered that the stated rate be updated annually. (*Id.*, p. 233)

In their Initial Brief, the Ameren Companies claim that because a fixed price QF rate would change annually, such an option would not help a QF customer evaluate the economics of constructing a QF installation or completing an interconnection. (Ameren IB, pp. 138-139) Staff witness Rockrohr considered this argument which was made by Mr. Jones in his rebuttal testimony and testified that it did not affect his recommendation. (Rockrohr Reb., ICC Staff Exhibit 20.0, p. 5) Despite the Ameren Companies' claim to the contrary, allowing QF customers to estimate a return on investment based on a known price per kilowatt-hour for a year is certainly more helpful to smaller QF operators/owners than basing the same decision on a price that is unknwown and that could vary hour to hour.

The Ameren Companies also argue that a fixed-price compensation option within Rider QF, would cause an imbalance between costs and revenue because the BGS-LRTP supplier forward contracts that the Ameren Companies adopted applies all QF energy purchases to Rider RTP-L load. The Ameren Companies argue that because the price paid to QF customers using the fixed price option might differ from the price paid through the supplier forward contract, a fixed price option would cause an imbalance between costs and revenue in every hour which the MISO LMP does not equal the fixed price option. (Ameren IB, p. 139) While Staff witness Rockrohr did not dispute that the price associated with a fixed price option might, during any hour, differ from the hourly price associated with the Ameren Companies' BGS-LRTP supplier forward contract, Mr. Rockrohr pointed out that during some hours the fixed energy price paid to QF's might be less, and during other hours it might be more than the BGS-LRTP supplier forward contract price and therefore over time a fixed price option would have very little effect on Rider RTP-L customers' energy costs. While the Ameren Companies provided no data in the record regarding the number of existing QF customers in each utility's service area, or the kilowatt-hours of QF energy each of the Ameren Companies purchase, they state in their initial brief "…the price disparity is likely to have a chilling effect on customers interested in Rider RTP-L". (Ameren IB, p.136) Staff would point out that this unsupported statement could only be true if: 1) a significant percentage of Rider RTP-L load were supplied by QF generation, 2) a significant percentage of that QF generation was purchased using the fixed-price compensation option, and 3) the Ameren Companies' dramatically overestimate their own avoided energy costs when setting the price for the fixed price option; but there is no evidence in the record to support those assumptions.

Finally, as discussed above Staff's recommendation regarding the Ameren Companies' Rider QF is essentially the same recommendation that Staff made with respect to ComEd's Rider POG. Given the Commission's recent order in ICC Docket No. 05-0597 regarding Rider POG, for consistency purposes the Commission should adopt Staff's recommendation for Rider QF.

F. Supply Procurement Adjustment

1. Recovery of supply-related costs

While at first the Ameren Companies appear to agree with the position of CNE/PES witnesses O'Connor and Domalgaski that all supply-related costs should be recovered through the SPA, its Initial Brief goes on to cite Mr. Cooper's testimony that costs to be included are those approved by the Commission, from time to time. (Ameren IB, p. 141) However, CNE/PES proposes that the Commission require Ameren to properly track and allocate all direct and indirect supply-related costs for recovery via the SPA. (CNE/PES IB, p. 2) Staff does not take issue with the specific amount proposed by the Companies for recovery through the SPA. (Staff IB, p. 148) With regard to the CNE/PES proposal, Staff does not agree that the costs have been sufficiently identified as being procurement related for recovery though the SPA.

However, Staff contends that to the extent the Commission finds such costs to be recoverable through the SPA, a corresponding decrease to the revenue requirement would need to be made. (*Id*., p. 149)

2. Amount of supply-related costs

The Ameren Companies are correct in saying that there is no dispute between Staff and the Companies concerning the amount of $812,857 power supply costs to be recovered through the SPA. (Ameren IB, p. 138) However, to state that "Respondents' Exhibit 36.14, Schedule 1, provides the amounts that have been specifically quantified and attributable for recovery by Staff or intervenors" is misleading. (*Id*.) BGS tariff support costs of $2,717,554 on line 3 of that schedule reflect the Companies' position. The substantiated amount of BGS tariff support costs that Staff proposes to be recovered through the SPA is $2.243 million. (Jones Reb., ICC Staff Exhibit 14.0, Schedule 14.02 (CIL), (CIPS), (IPC))

Also misleading is that the amount of $812,857 on line 2 of Respondents' Exhibit 36.14, Schedule 1, reflects an annual amount, but the amount on line 3 reflects a total amount. The Ameren Companies agree that, regardless of the recovery mechanism, BGS tariff support costs recovered should be amortized over a three-year period. (Tr., pp. 490-491) Therefore, the amount on line 3 of Respondents' Exhibit 36.14, Schedule 1 should reflect one-third of the total amount of BGS tariff support costs approved by the Commission. Based on Staff's proposed amount of $2.243 million, line 3 should be $747,667 and the total Supply Procurement Adjustment allocated among the Ameren Companies should be $1,560,524 ($812,857 + $747,667). (Staff IB, p. 149)

3. SPA tracking through the Market Value Adjustment Factor

The Ameren Companies continue their argument that “preciseness” in recovery of supply-related costs is in the best interest of all stakeholders. (Ameren IB, p. 144) However, the Companies also continue to fail to explain how precision can occur when costs from a test year are recovered based on actual sales data from a different period. The Companies propose that a test year level of costs be approved for recovery through the SPA. (Stafford Dir., Ameren Ex. 6.0S, p. 2) The MVAF as approved in the procurement proceeding is to ensure equality between amounts paid to suppliers and amounts billed to customers. Tracking the SPA through the MVAF would not ensure SPA costs *incurred* are equal to SPA costs billed, but would compare defined costs set in a past test year with actual amounts recovered from customers in the current period. In order to achieve the kind of true-up the Ameren Companies seek, one must reconcile costs actually incurred in a particular period with recoveries for that same period. Instead, the Ameren Companies’ proposal 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. (Staff IB, p. 150) The “true-up” of SPA costs through the MVAF is nothing more than a novel ratemaking theory to attempt to collect a relatively insignificant amount through a rider, and thus should not be approved.

G. Line Extension Refunds

Staff witness Rockrohr objected to the line extension provisions that the Ameren Companies propose because those provisions do not comply with Part 410. (83 Ill.

Adm. Part 410) The Ameren Companies are proposing their line extension provisions "in lieu of 83 Ill. Administrative Code Part 410", and Mr. Rockrohr explained that Subsection 410.410(a)(2) requires that line extension provisions made in lieu of 83 Ill. Administrative Code Part 410 must be "…generally more favorable to applicants than the provisions of subsections (b) and (c)." (83 Ill. Adm. Part 410, Section 410.410 (a)(2)) (Staff IB, pp. 152-153) The Ameren Companies' proposed line extension provisions are not generally more favorable than the line extension provisions described in subsections (b) and (c) because the Ameren Companies' line extension provisions significantly reduce the period of time an applicant's refundable deposit is subject to refund: from ten to five years. (*Id.*, p. 152)

Mr. Rockrohr explained that an applicant would only receive a refund of a line extension deposit if the Ameren Companies later utilize the same line extension to supply additional applicants. Since the Ameren Companies' proposed provisions allow refunds for only a five year period instead of a ten year period, the likelihood that the original applicant will receive a refund is tremendously reduced. Therefore, the Ameren Companies' extension provisions are not generally more favorable to applicants than the provisions of Section 410.410 subsection (b) and (c), do not comply with Subsection 410.410(a)(2), and should not be approved. (Rockrohr Dir., ICC Staff Exhibit 9.0, pp. 4-7) (Staff IB, p. 153)

The Ameren Companies' contend that other aspects associated with their proposed line extension provisions caused their line extension provisions to become generally more favorable to applicants than the Commission's provisions. Mr. Rockrohr provided reasons, despite the Ameren Companies' contention, that was not the case:

- The Ameren Companies stated their provisions would give residential applicants an option to reduce the upfront charge in return for making the payment become nonrefundable. (Ameren IB, p. 141) Mr. Rockrohr pointed out that an option to reduce the upfront charge in return for making the payment become nonrefundable would only benefit applicants if no other applicants utilized the line extension. (Rockrohr Reb., ICC Staff Exhibit 20.0, p. 9) Ameren witness Carls responded, "He is correct in that regard, but we have found in limited use of this concept that applicants have a pretty good idea of whether someone else will be utilizing that extension in the near future and often opt for the benefit of paying less upfront and foregoing the tracking/refunding possibility." (Carls Sur., Respondents' Exhibit 51.0, p. 2) Mr. Carls' statement in surrebuttal testimony illustrates Mr. Rockrohr's point that this option would only benefit those customers if no other applicant were to utilize the same extension during the entire refund period. Even applicants that "have a pretty good idea" whether someone else will utilize the line extension "in the near future" would not know about all potential development that could utilize the line extension over the next 5-10 years.
- The Ameren Companies state their extension provisions include a change in the demarcation point for facilities to be considered "line" or "service". The demarcation point between "line" and "service" is to be the customer's property line, which the Ameren Companies state will result in more of the extension meeting the definition of "service" instead of "line". (Ameren IB, p. 143). In rebuttal testimony Mr. Rockrohr agreed that if an applicant's line

extension footage were reduced as a result of the new demarcation point, then it would be logical that the service extension would become longer. Mr. Rockrohr pointed out that the applicant's non-refundable deposit would likely increase as a result of the longer service, while the applicant's refundable deposit for the line extension would likely decrease. Depending on the specifics of the installation, the Ameren Companies' new demarcation point might cause an applicant's initial costs to increase, decrease, or stay about the same. However, the percentage of the applicant's payment that is nonrefundable would only increase. (Rockrohr Reb., ICC Staff Exhibit 20.0, pp. 9-10) Ameren witness Carls responded in surrebuttal testimony: "It is my belief that this change will result in charges being moved from "line" to "service", and historically the costs for service extensions are almost always lower than for line extensions." (Carls Sur., Respondents' Exhibit 51.0, p. 2) Mr. Carls failed to address the fact that the associated increased fees applicants pay for service extensions as a result of the change in demarcation point are all nonrefundable.

- The Ameren Companies state their provisions give residential applicants an option to install conduit for service extensions and possibly for some line extensions, which could reduce the amount of payment required. (Ameren IB, pp. 141-142) In other words, if the applicant trenches and installs the conduit on applicant's own property, the Ameren Companies *might* reduce the nonrefundable service charge. Mr. Rockrohr pointed out that a potential reduction in the service charge in exchange for the applicant providing labor and materials that would normally be provided by the Ameren Companies had nothing to do with the Ameren Companies' treatment of the applicant's deposit for the line extension. (Rockrohr Reb., ICC Staff Exhibit 20.0, p. 10) In response, Mr. Carls simply reiterated that the Ameren Companies would reduce the service charge to the applicant in exchange for the applicant's trenching and installing service conduits. (Carls Sur., Respondents' Exhibit 51.0, pp. 2-3)

Surprisingly, the Ameren Companies stated that "all of Mr. Rockrohr's claims were soundly refuted". (Ameren IB, p. 142) Staff is confused by this assertion. In actuality, as described in the above bullet points, none of Mr. Rockrohr's “claims” were refuted, and the Ameren Companies' testimony either confirmed the validity of Mr. Rockrohr’s “claims” or did not address them.

Mr. Rockrohr recommended that, instead of making their provision "in lieu of" the Commission's line extension provisions, the Ameren Companies offer applicants the choice of utilizing the Ameren Companies' line extension provision or the Commission's line extension provisions, as provided in Subsection 410.410(a)(1). Mr. Rockrohr pointed out that doing so would eliminate the compliance issue associated with the line extension provisions that the Ameren Companies filed. (Rockrohr Dir., ICC Staff Exhibit 9.0, p.9) (Staff IB, p. 155)

The Ameren Companies misrepresented Mr. Rockrohr's recommendation in their initial brief by stating, "Implicitly realizing the merits of the proposal, Staff witness Rockrohr suggested that the Ameren Companies offer both, that is, offer the package of options but also be required to continue to track refunds over a 10 year period of time."

(Ameren IB, p. 142) This statement is blatantly wrong. Mr. Rockrohr's recommendation was that, rather than wording their provision so that it was "in lieu of Part 410", which causes the provision to be non-compliant with Subsection 410.410(a)(2), the Ameren Companies word their provision so that the applicant will have a choice of obtaining the extension under either the Ameren Companies' provisions or obtaining the extension under the Commission's provisions as provided in Section 410.410 subsections (b) and (c). Thus the line extension provision would no longer fall under Subsection 410.410(a)(2), but instead would fall under and comply with Subsection 410.410(a)(1) while still providing the Ameren Companies a 5-year refund tracking for those customers that choose the Ameren Companies' provisions. (Rockrohr Dir., ICC Staff Exhibit 9.0, p.9) (Staff IB, p. 155)

In response to Mr. Rockrohr's recommendation, the Ameren Companies indicated that rather than providing applicants with the choice of using either the Ameren Companies' or the Commission's line extension provisions, they would prefer simply tracking all refundable deposits for line extensions for 10 years. (Carls Sur., Respondents' Exhibit 51.0, p.3) Staff has stated it would not object to the Ameren Companies' alternative proposal to change the refund tracking period to 10 years for line extensions while continuing to make its line extension provision "in lieu of" Section 410.410 subsections (b) and (c). (Staff IB, p. 156)

As a last resort, the Ameren Companies threaten to eliminate the options associated with their line extension provisions that they previously claimed would be beneficial to applicants if the Commission determines that Staff is correct on this issue. (Ameren IB, p.142) The Commission should ignore this threat, the Ameren Companies' proposed provisions do not comply with the Commission's rules, and for that reason alone the Commission should not allow them to become effective.

H. Residential RTP Program

Ameren does not oppose CUB's residential Real Time Pricing ("RTP") proposal under which metering and administrative costs associated with the selection of RTP by up to 20,000 residential customers would be spread over the entire residential customer base. (Ameren IB, pp. 142-144) These costs are estimated at $1,484,531. (*Id.*, p. 143) Customers participating in the RTP program would take service under Rider ESP (Schedule 41.3). (*Id.*)

Ameren believes that Rider ESP could meet the requirements of the recently enacted Public Act 94-0977. Public Act 94-0977, in particular Section 16-107 (b-5) (220 ILCS 5/16-107(b-5)), requires the Commission to review tariffs filed in response to that legislation from a net benefits perspective. Staff's position is that Ameren has not supported Rider ESP with evidence about the potential benefits of the implementation of residential RTP that are listed in Public 94-0977, nor has it provided a net benefits calculation. (*Id.*) Therefore, Rider ESP should not be approved and the proposed addition of $1,484,531 should not be added to Ameren's revenue requirement. (Staff IB, pp. 158-159)

I. Other

V. MISCELLANEOUS SERVICE ISSUES

A. Line and Service Extensions

B. Metering Services

C. Vegetation Management/Tree Trimming[12]

The Ameren Companies begin their argument in this section by mischaracterizing Staff testimony and making a vague but incorrect legal assertion. The Ameren Companies assert that "Mr. Spencer testifies that Staff began interpreting Rule 218 as a no-contact rule in October 2002. (ICC Staff Exhibit 21.0, p. 10, line 215.)" (Ameren IB, p. 157) Mr. Spencer did not testify that Staff "began interpreting NESC Rule 218 as a no-contact rule in October 2002." Mr. Spencer only testified that Staff's position was stated in documents going back to October 2002:

> In addition to the above Ameren-related documents, there have been several others related to other Illinois companies (including Illinois Power before merging with Ameren) in which Staff's "no contact" position was stated, going back as far as October 2002.

(Spencer Reb., ICC Staff Exhibit 21.0, p. 10)

Having concocted a fact not supported in the record, the Ameren Companies then assert that "Staff's attempted new interpretation of NESC Rule 218 constitutes illegal rulemaking." (Ameren IB, p. 157) This argument is nothing but a red herring. Staff's interpretation of NESC Rule 218 as adopted in Part 305 to require tree trimming consistent with a no-contact policy is either right or wrong. If Staff's position is correct,

[12] Staff has already responded to some of the Ameren Companies' arguments concerning tree trimming issues in Section II.B. above, and will not repeat those arguments here. Staff responds here to new or additional arguments raised at pages 156 to 162 of the Ameren Companies' Initial Brief.

and Staff asserts that it is, then there is no “illegal rulemaking”. The Commission is all too familiar with the fact that the meaning of rules and statues is litigated all the time, and resolution of issues concerning the meaning of language does not constitute illegal rulemaking.

Staff must also point out that it is not surprising that the “no-contact” issue is arising at this time. As the reliability reports introduced into the record in this proceeding demonstrate, Staff has been working to improve tree trimming practices for some time. Indeed, a four-year tree trimming cycle was only achieved as recently as 2004. (Staff IB, p. 167) There simply was no reason to focus on “no-contact” when utilities were not even achieving a four-year trimming cycle. More frequent trimming cycles have been achieved through the work of both utilities and Staff, and the potential for full compliance with the requirements of the Commission’s tree trimming rule is within reach. Staff should not and cannot be faulted for its diligent and reasonable efforts to bring utilities’ tree trimming practices into full compliance with the Commission’s tree trimming rules.

The Ameren Companies spend much time presenting Mr. Clapp’s personal interpretation of NESC Rule 218. (Ameren IB, pp. 157-160) These arguments are misplaced and inappropriate. The “primary rule of statutory construction is to give effect to legislative intent by first looking at the plain meaning of the language.” (*See e.g.,* Davis v. Toshiba, 186 Ill. 2d 181, 184-85 (1999)) The Ameren Companies ignore this tenant in focusing on Mr. Clapp’s personal understanding of NESC Rule 218 to the exclusion of the actual language at issue. Further, at issue here is the meaning of the language of NESC Rule 218 as adopted by the Commission in Part 205. First, the

Commission's rules make clear that "[n]o incorporation in this Part [of the NESC] includes any later amendment or edition." (83 Ill. Adm. Code 305.20(c)) Similarly, the Commission's rules specify that "[f]ootnotes and notes which reference provisions of the NESC which have not been expressly adopted by the Illinois Commerce Commission shall not be construed to incorporate such provisions into this Part." (83 Ill. Adm. Code 305.110(a)) Mr. Clapp's testimony is directly contrary to both of these provisions, referencing both un-adopted portions of the NESC and subsequent enactments. (See Ameren IB, pp. 158-159 (referring to NESC Rule 010 in Section 1 and 2006 updates))

D. Other

1. Staff's Reports on Service Reliability

The Ameren Companies' contend that Staff's testimony on service reliability should somehow be disregarded because "Staff does not normalize for weather-related outages in assessing reliability." (Ameren IB, p. 161) The Ameren Companies further assert that the Commission's rules require taking weather and other uncontrollable events into account when assessing a system's reliability. (*Id*., pp. 161-162)

First, the Commission's rules do not provide for adjusting the reported reliability statistics, SAIFI, CAIDI, or CAIFI, to eliminate the effects of storms. Staff uses these statistics in its analysis of utility electric service reliability, but also considers the causes for the interruptions, as reported by the utilities. When evaluating the reliability performance and the utility's remedial action plans for worst performing circuits, for example, Staff considers the interruptions attributed to weather, as well as all other reported causes, to determine if the utility's remedial actions seem appropriate. Second, the rule provisions cited by the Ameren Companies only provide that the

Commission “shall consider” such events, but do not dictate how the Commission shall treat such events in evaluating reliability. In other words, contrary to the Ameren Companies’ assertion, the Commission is not required to disregard or discount weather related outages While this is something the Commission may do, it is not required to – it only need consider such events under Commission’s rules.

VI. RESPONSES TO COMMISSIONERS’ QUESTIONS

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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