STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

CENTRAL ILLINOIS LIGHT COMPANY	:	
d/b/a AmerenCILCO	:	
	:	No. 06-0070
CENTRAL ILLINOIS PUBLIC SERVICE COMPANY	:	
d/b/a AmerenCIPS	:	
	:	No. 06-0071
ILLINOIS POWER COMPANY	:	
d/b/a AmerenIP	:	
	:	No. 06-0072
Proposed general increase for delivery services	:	(Consolidated)
(Tariffs filed December 27, 2005).	:	

APPENDIX TO IIEC'S BRIEF ON EXCEPTIONS

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EXCEPTION 1

III. Rate Base

D. General and Intangible Plant

4. Commission Conclusion

Ameren has proposed to increase CILCO's, CIPS', and IP's G&I plant from the amount approved in each of the utility's last rate case. The increase proposed for CIPS is from $52.3 million to $121.9 million, a rise of $69.6 million or 133%. For IP, Ameren proposes to increase G&I plant by $72.2 million, or 54%, from $134.3 million to $206.5 million. Ameren further proposes an increase for CILCO's G&I plant of $13.2 million, or 46%, from $28.9 million to $42.1. Staff has proposed to reduce the rate base of CIPS by $61.1 million, and IP's rate base by $123.6 million, but proposes an increase of G&I plant for CILCO of $13.7 million. Staff bases its proposed disallowance on what was removed from each utility's rate base in its last rate case, and which Staff believes Ameren is attempting to add back. IIEC also opposes Ameren's increases and suggests that G&I plant only increase by the same percentage as is allowed for distribution plant.

The Commission notes that Ameren indicates that it has attempted to allocate costs by way of its ASP. The details of this project are discussed earlier in this Order, and need not be repeated. The gist of the project is that Ameren claims that it has allocated the cost of each item of G&I plant to the function it supports, or between various functions, if it supports multiple areas. However, the ASP does not address or explain the substantial difference between the level of G&I plant the Commission found to be just and reasonable in the delivery service cases for the Ameren Companies and this case.

As regards IIEC's proposal regarding G&I, the Commission first notes that this same argument was advanced by IIEC in the ComEd DST case, Docket No. 05-0597, and initially rejected. However, rehearing has been granted in that case on this issue. Therefore it is not clear whether IIEC's position will be rejected on rehearing. Also, the Commission agrees with the arguments made by IIEC in its Brief on Exceptions that this case is somewhat different than the ComEd case. ~~While this argument has a certain simplicity to it, without some~~ ~~overriding~~ Absent a full explanation of the substantial increase in G&I plant in this case circumstances necessitate~~ing~~ the use of this proportionality concept recommended by IIEC. ~~, the Commission does not see the need to apply this concept in this matter.~~

~~Staff's arguments on this issue are simply lacking. While Staff points out the reductions made to G&I plant in earlier dockets and argues that these same reductions should be made again, as noted on this issue in Docket No. 05-0597, each docket should be reviewed on its own merits. Staff fails to point out any specific assets which have been inappropriately assigned to G&I, or which were previously excluded from G&I~~

~~and which Ameren is now attempting to add back in. While it is correct that the burden is not on Staff to justify the level of G&I costs proposed, the Commission finds Staff's evidence on this issue wholly unpersuasive. Staff's evidence, or the lack thereof, showing any errors contained in Ameren's ASP methodology or application, is insufficient to discount the ASP finding. In the absence of contradictory evidence, the Commission is satisfied that Ameren, by use of the ASP, has properly allocated G&I costs for CILCO, CIPS, and IP and concludes that the proposed G&I costs are appropriate.~~

EXCEPTION 2

IV. Operating Expenses and Revenues

E. A&G Expense

1. Functionalization

e. Commission Conclusion

Ameren proposes increases in A&G expenses for each of its Illinois utilities. These proposed increases range from a 63.8% increase for CIPS, to a 394.3% increase for CILCO. Across the three utilities, the proposed increase totals 210%. Ameren indicates that it determines how A&G expenses are allocated based on which utility the work is performed for. Ameren adds that if an employee routinely works for more than one company, then that employee is transferred to Ameren Services, in which case their time reporting is governed by the GSA. Ameren attributes the increases in A&G expenses to increases in pension and major medical costs, along with increased security costs since September 11, 2001, and increased reporting requirements under Sarbanes-Oxley. Ameren submits that the proposed A&G expense level is appropriate and in line with proposed O&M costs.

Staff, IIEC, and Wal-Mart all oppose the level of increase in A&G expenses proposed by Ameren. Wal-Mart suggests that the Commission adjust Ameren's A&G expenses to reflect normalized levels of pension and OPEB expense. As the Commission does not accept Wal-Mart's position on pension and OPEB expense, the Commission will not adopt Wal-Mart's position here.

IIEC takes the position that any increase in Ameren's A&G expense should be limited to the approved increase in O&M expense. IIEC submits that there is a proportional relationship between these two expense amounts which the Commission has recognized in prior delivery services cases, and which should be maintained in this proceeding. ~~While r~~Recognizing that the proposed increases in A&G expenses far outstrip the proposed increases in O&M expenses, the Commission believes that Ameren has not made a sufficient showing as to the reason for these increases and ~~rejects~~ accepts IIEC's proposed adjustments.

As a percentage, the increases in A&G expenses for each company are ~~might seem~~ excessive. The Commission recognizes~~, however,~~ that changes have occurred in the landscape for each utility. However, those changes do not fully explain the substantial increase in A&G expense.~~IP has now been acquired by Ameren, and is operating within an entirely different operating system. CIPS has acquired the assets of UE, and incorporated those employees.~~ Additionally, as discussed later in this Order, while there has been a significant increase in pension and OPEB expense for each

company those increases alone do not explain the proposed increase in A&G expense in this case.

~~The Commission notes that Ameren and Staff are in agreement as to the appropriate A&G expense level for CILCO of $31.202 million, and are also in agreement as to the appropriate level of A&G expense for CIPS of $42.735 million. Staff has proposed a downward adjustment to IP's A&G expenses, based on specific adjustments recommended by Ms. Jones. The Commission is satisfied that Staff's recommended adjustments to the A&G expense levels for CILCO and CIPS are appropriate, and they will be adopted, subject to any specific expense adjustments discussed elsewhere in this Order. For IP, the individual adjustments to A&G expense levels are addressed later in this Order. The overall amount of A&G expenses included in the Appendices reflects those adjustments that are approved as well.~~

EXCEPTION 3

IV. Operating Expenses and Revenues

F. Effect of Ameren Ownership on IP Expenses

4. Commission Conclusion

IIEC and the AG each propose separate adjustments related to the effect of Ameren ownership on IP expenses. Ameren opposes both adjustments.

IIEC proposed an adjustment based on the belief that Ameren has not met its commitments with respect to estimated synergy savings resulting from Ameren's purchase of IP. In the Commission Order approving the purchase of IP by Ameren, the Commission authorized the amortization of approximately $67 million from 2007 to 2010 for certain merger costs, conditioned on Ameren showing that IP is taking adequate steps to produce savings and to take measures to insure that rates are not increased if savings fail to materialize. Ameren has proposed a test year amortization expense of $12.184 million related to these merger costs. IIEC submits that Ameren has failed to show that it has achieved the anticipated savings, and that full recovery of this amortization of expenses would have an adverse rate effect on IP customers. IIEC proposes that the Commission authorize IP to recover only $3.883 million in merger costs for the test year; the amount IIEC suggests has been offset by achieved test year savings. Ameren submits that IP has satisfied the required conditions of Docket No. 04-0294, and that IP should be allowed to amortize the recognized costs in full. The Commission is not satisfied that IP has complied with the ~~appropriate~~ substantive meaning of the conditions of Docket No. 04-0294 related to synergy savings, and will not adopt the disallowance proposed by IIEC on this issue. Section 7-204 requires that the Commission find that adverse rate impacts are unlikely as a precondition to its approval of a proposed merger. The Commission would undermine that requirement if it approved a merger based, in part, on empty conditions that did nothing to effect its expectation of no adverse impacts on retail customers. Reading the requirements of the Docket 04-0294 Order in that light, IP's report filings, without achieved savings to offset the claimed merger expenses, does not meet the ordered merger conditions.

The AG proposes a reduction in Ameren's test year expense related to Ameren Services costs of $4.666 million. Each party's arguments are set out above, with the essence of Ameren's argument being that while this proposed cost is higher than envisioned in the Ameren/IP merger docket, the costs reflected in Docket No. 04-0294 need to be adjusted upward, for factors such as inflation, wage increases, to reflect Dynegy's business difficulties, and to reflect 12 months of expense, rather than 9 months. The AG argues that the expenses for the merger year were known by the parties, and that to adopt IP's upward adjustments would obviate the Memorandum of Understanding entered between the parties in Docket No. 04-0294.

The Commission is of the opinion that the AG's arguments are correct regarding this expense. Ameren has not shown a sufficient reason for the Commission to depart from the understandings which were contained in Docket No. 04-0294 to approve the acquisition of IP by Ameren. The Commission will therefore adopt the AG's proposed reduction in test year O&M for expense.

EXCEPTION 4

V. Rate of Return

B. Capital Structure

6. Commission Conclusion

The parties all seem to agree that determining the cost of capital is not a precise science. The Commission concurs and believes that when ~~so long as the~~ the cost of common equity adopted by the Commission is consistent with the capital structure adopted, the result will produce just and reasonable rates. Consequently, ~~In the Commission's view, while the capital structure is important,~~ there is no single perfect capital structure for ratemaking purposes. In this case, the Commission will follow its long-standing practice for determining the authorized rate of return on rate base. First, the Commission will establish a reasonable capital structure and subsequently establish an authorized return on common equity that is consistent with the financial risk inherent in the capital structure adopted.

IIEC recommends that the Commission adopt an imputed corporate capital structure for assessing IP's riskiness, and CUB recommends the use of imputed capital structures for CILCO, CIPS, and IP. IIEC and CUB argue, essentially, that imputed capital structures are required because Ameren's actual capital structures contain too much common equity which improperly increases the overall cost of capital.

Ameren and Staff oppose the use of imputed capital structures. They argue, essentially, that the capital structure of each Ameren utility is reasonable and that in the current situation imputing a capital structure is not warranted.

As the Commission understands it, Ameren and Staff are proposing the that following capital structures be used for setting rates in this proceeding:

Ameren's Proposal		Staff's Proposal	
CILCO		**CILCO**	
Long-term debt	28.25%	Long-term debt	29.67%
Short-term debt	9.58%	Short-term debt	16.13%
Preferred stock	8.88%	Preferred stock	8.63%
Common equity	53.29%	Common equity	45.57%
Total	100.00%	**Total**	100.00%
CIPS		**CIPS**	
Long-term debt	46.04%	Long-term debt	46.12%
Short-term debt	0.42%	Short-term debt	0.33%
Preferred stock	4.62%	Preferred stock	4.63%

Common equity	48.92%	Common equity	48.92%
Total	100.00%	**Total**	100.00%

IP		**IP**	
Long-term debt	30.16%	Long-term debt	30.97%
TFTN	14.47%	TFTN	15.41%
Short-term debt	0.09%	Short-term debt	0.00%
Preferred stock	2.21%	Preferred stock	2.06%
Common equity	53.07%	Common equity	51.56%
Total	100.00%	**Total**	100.00%

For IP, CUB proposes a common equity ratio of 41.46% and IIEC proposes a common equity ratio of 42.3%. The capital structures proposed by Ameren and Staff for IP are intended to be actual capital structures and, in the Commission's view, are similar. Ameren and Staff do not propose distinct capital structures for credit assessment and for ratemaking.

Both Ameren and Staff ~~suggest~~ acknowledge that imputed capital structures may be appropriate in some situations. ~~but not in this situation for IP.~~ They argue ~~They suggest~~ that the Commission should first review the actual capital structure and only in the event it is ~~deemed~~ found unreasonable should the Commission then impute a reasonable capital structure. IIEC argues ~~seems to believe~~ that this process shifts the burden from the utility to demonstrate that its actual capital structure is reasonable to other parties to demonstrate it is not reasonable. Nevertheless, IIEC demonstrated that AmerenIP's actual capital structure is in fact unreasonable for setting rates. ~~The Commission is not persuaded by IIEC's argument.~~

In setting rates, the Commission must start somewhere. That starting point is the testimony and data that accompany a utility's tariff filing which typically reflects an actual capital structure recommended by a utility witness. As IIEC points out, ~~Contrary to IIEC's suggestion,~~ the utility has the burden to demonstrate its proposed capital structure is reasonable. In this case, ~~not only does~~ Ameren presents some evidence in support of IP's actual capital structure, so does a Staff expert witness. However, the bulk of that evidence concerns a dispute between Ameren and Staff as the proper period for defining the competing "actual" capital structures they propose. In this Order, the Commission must ~~will~~ evaluate that evidence on an equal footing with the evidence presented by other parties to determine the appropriate capital structure, based upon the evidence in the record and the arguments in the briefs. If any presumption favoring the reasonableness of the "actual" capital structure presented by Ameren ever played a role here, it ended once contrary evidence was introduced. Under Illinois law, any such presumption vanishes completely when contrary evidence is produced.

IIEC argues that IP's "corporate" capital structure, when adjusted to exclude the ~~excluding~~ TFTNs, which credit rating agencies do not consider in evaluating the Ameren utilities riskiness, the percentage of capital represented by equity is too large. ~~contains~~

too little debt. Given the emphasis Ameren has placed on maintaining the appropriate credit rating, this is a pertinent inquiry. The Commission is satisfied that the removal of TFNs for this purpose is appropriate. Recalculating the debt and equity component percentages reveals a very large equity component. That percentage exceeds the ratios indicated under credit rating agency guidelines to maintain its credit rating, and it is excessive in comparison to the comparable risk proxy groups used to estimate Ameren's cost of equity. that this proceeding will establish a ratemaking capital structure and that this capital structure will include TFTNs, the Commission gives little consideration to these arguments by IIEC.

Both IIEC and CUB suggest that the Commission, both generally and specifically in this case, should closely examine any approve capital structures that are indicative of consistent with credit ratings of no higher than BBB. The Commission will not adopt such a policy as a cap on allowed returns, but close scrutiny is appropriate. As the Commission understands it, there is a complex nonlinear relationship between financial leverage and the required rate of return. The Commission does not believe it is easy to determine an optimal capital structure or correct bond rating. The Commission understands that reducing financial risk reduces the cost of debt as well as the cost of common equity. The Commission also is aware that reducing financial risk comes at a cost to ratepayers and that it must balance the competing objectives. suggestion that a BBB bond rating is "correct" either generally or in this specific case is simply not supported by the record.

Having reviewed the evidence and arguments, the Commission finds that IP's actual capital structure contains more equity than is necessary to maintain its current credit rating, and that the AmerenIP capital structure proposed by IIEC, which adjusts the TFNs, the Commission finds further that including the TFNs in the ratemaking capital structure accurately reflects the lower cost of the capital acquired through TFNs and is reasonable for purposes of setting electric distribution rates in this proceeding, provided an appropriate cost of common equity is adopted. Expert witnesses for both Staff and Ameren testified in support of IP's capital structure. Those The arguments, of CUB and IIEC's witnesses, while well stated, simply do not convince the Commission that it is necessary to permit earnings on such a high impute a lower percentage of common equity to produce a reasonable rate of return on rate base.

If the Commission were to impute additional debt into IP's capital structure, it might then become necessary to make adjustments to IP's embedded cost of debt. As previously stated, the Commission believes it is tantamount that the adopted capital structure be consistent with the adopted costs for the sources of capital. Imputing a corporate capital structure like that recommended by IIEC means that rates will be set using a risk assessment capital structure that is appropriately similar to those of the proxy groups used to estimate Ameren's cost of common equity. The Commission adopts IIEC's capital structure recommendations for AmerenIP. would complicate determining an appropriate rate of return on rate base by adding the possibility of measurement error to determining the cost of debt. In sum, given the record in this proceeding and the complexities in determining the appropriate rate of return on rate

~~base, the Commission concludes that IP's actual capital structure is appropriate for purposes of this proceeding, provided that the Commission adopts appropriate cost rates.~~

Given the conclusion immediately above, the Commission must address the dispute between Ameren and Staff regarding the appropriate measurement period for IP's capital structure. Staff proposes using IP's December 31, 2004 capital structure while Ameren proposes measuring IP's capital structure at December 31, 2005.

Among other things, Staff argues that advancing the measurement period for IP to 2005 complicates the analysis because it becomes necessary to evaluate adjustments for fair value purchase accounting made during 2005. Staff also raised concerns about the accuracy of IP's proposed December 31, 2005 capital structure due to the limited time availability and Ameren's propensity to make errors in this proceeding. Ameren argues that having consistency among the dates used to establish the capital structures of CILCO, CIPS, and IP is desirable. Ameren also suggests that the capital structure for IP should reflect the fair value purchase accounting adjustments made during 2005, a view that Staff does not share.

Having reviewed the arguments of Staff and Ameren, the Commission observes that this is a close call and, with slightly different circumstances, could easily go either way. The determinative factor here is that Ameren originally proposed to use a December 31, 2004 capital structure for IP. December 31, 2004 was a reasonable measurement period when Ameren originally filed its tariffs and the Commission believes it is still reasonable. The one argument to which the Commission gives little weight is that it is important or useful to have the same measurement date for CILCO, CIPS, and IP. While the Commission believes that consistency is sometimes important, that concept has little value in establishing capital structures for three separate utilities. Ideally a review of Ameren's fair value purchase adjustments would have been possible as well, nevertheless, the Commission was underwhelmed with several aspects of Ameren's rate case presentation and is unwilling to accept the proposed change to IP's capital structure at the rebuttal stage of the proceeding.

The final issue with regard to IP's capital structure is whether the average balance of short-term debt should be centered upon the capital structure measurement date as Staff recommends or should end at the same date as the capital structure measurement period as Ameren recommends. The Commission is somewhat dismayed that Ameren and Staff continued to argue over this issue throughout the course of this proceeding. The Commission has reviewed its recent decisions in IP and Ameren rate cases and did not find a case where the issue was addressed. The Commission believes that may be because, all things considered, it is not significant.

Neither Ameren's nor Staff's approach could be considered totally unreasonable. Any advantage to either utility shareholders or customers derived from one method or the other would depend upon the specific circumstances present in any case. The Commission believes the largest risk associated with this relatively insignificant issue is

that by switching between approaches either utility shareholders or utility ratepayers would be treated unfairly. The Commission observes that in a relatively recent rate case the Commission adopted the approach advocated by Staff. (Docket Nos. 03-0676/03-0677 (Cons.), October 6, 2004 Order at 20-21) Thus, the Commission adopts Staff's methodology for calculating short-term debt balances in this proceeding.

The next issue facing the Commission is whether CIPS' actual capital structure containing approximately 49% common equity and approximately 46% long-tem debt is unreasonable and contributes to an overall cost of capital that is too costly. CUB proposes an imputed capital structure with approximately 28% common equity and 67% long-term debt. The bases for CUB's proposal regarding CIPS' capital structure are essentially the same as its proposal for IP. The only distinction in CUB's arguments that the Commission can identify is that CIPS is in a somewhat stronger financial position than IP.

Based upon an analysis of CIPS' financial position, Staff concludes that while it is possible that CIPS' capital structure might be unnecessarily costly, it is not clear that the actual capital structure is inappropriate. IIEC does not take issue with Ameren's proposed capital structure for CIPS. The Commission believes that CUB has proposed to impute an excessive proportion of debt into CIPS capital structure. Based upon its review of the record and the complexities in determining the appropriate rate of return on rate base, the Commission finds that CIPS' actual capital structure is appropriate for purposes of this proceeding. The parties' positions regarding CILCO's imputed capital structure are essentially the same as those regarding CIPS' capital structure. As a result, the Commission's conclusion is the same. All things considered, the Commission finds that CILCO's actual capital structure is appropriate for setting rates in this proceeding.

Ameren proposes to measure CILCO's and CIPS' actual capital structures at December 31, 2005 while Staff proposes a measurement date of June 30, 2005. Because the Commission did not accept Ameren's proposal to measure IP's capital structure at December 31, 2005 the argument that measuring CIPS' and CILCO's capital structure at the same date carries no weight. Additionally, the Commission has previously determined for IP that using a short-term debt balance centered on the measurement date for the long-term capital balances is appropriate. This would not be possible if a December 31, 2005 capital structure were adopted. Thus, based upon the record in its entirety, the Commission adopts June 30, 2005 as the date for measuring CILCO's and CIPS' long-term capital balances and adopts Staff's proposed method for calculating the short-term debt balance.

Ameren also proposes a $100 million pro forma adjustment to CILCO's short-term debt balance. Ameren argues that a May 2005 equity infusion was made to permanently eliminate short-term debt. Staff counters that the $100 million reduction in short-term debt balance was only temporary and that CILCO's short-term debt balance began increasing shortly thereafter. It appears to the Commission that while in May 2005 the common equity balance for CILCO was permanently increased, CILCO's

short-term debt balance was only temporarily decreased. The evidence indicates that this is the case and such a result would be logical. Thus, by selecting June 30, 2005 for measuring CILCO's capital structure the Commission has captured the permanent increase in common equity balance. By rejecting Ameren's proposed pro forma adjustment to CILCO's short term debt balance and accepting Staff's proposed measurement period, the Commission believes the resulting short-term debt balance is reasonable for ratemaking purposes.

The final issue to be addressed in this portion of the Order is the dispute between Ameren and Staff over issuance expenses related to CILCO's $4.64 Series preferred stock. Preliminarily, it is not clear to the Commission that this is actually a capital structure issue but instead appears to relate to CILCO's embedded cost of preferred stock. Additionally, the Commission is surprised that Ameren and Staff continue to argue about this issue as the actual impact on CILCO's revenue requirement is immaterial. In short, this appears to be a waste of time and resources.

Nevertheless, the Commission has reviewed the evidence and the record does not support including in CILCO's revenue requirement the issuance expenses associated with CILCO's $4.64 Series preferred stock. The Commission could address Ameren's arguments point by point; however, in light of the record, to do so would only waste further time and resources on an issue that deserves essentially none. The Commission adopts Staff's proposed cost of preferred stock for CILCO, 5.38%.

EXCEPTION 5

V. Rate of Return

C. Measurement Date for Short-Term and Variable Interest Rates

3. LGI's ~~and IIEC's~~ Positions

~~The Commission notes that IIEC witness Gorman also proposed the use of a recent six-month average for the costs of variable rate long-term debt and short-term debt.~~

4. Commission Conclusion

~~IIEC witness Gorman recommends that a recent six-month average should be used for the variable rate pollution control bonds and short-term debt rather than the interest rate for these securities on any one specific date. A similar approach is endorsed by~~ LGI~~.~~ endorses an approach where a recent six-month average should be used for the variable rate pollution control bonds and short-term debt rather than the interest rate for these securities on any one specific date. Staff recommends measuring the cost of short-term debt and variable interest rate debt at April 4, 2006 while Ameren recommends measuring the costs at May 19, 2006.

The ~~IIEC and~~ LGI recommendation to use average cost rates rather than spot rates are rejected. The Commission believes that spot rates for estimating the cost of short-term and variable rate debt instruments are generally superior to average rates. ~~Neither IIEC nor~~ LGI has not provided a compelling reason for the Commission to deviate from its past practice on this issue.

Generally speaking, the Commission favors measuring all of the costs of capital at or over the same period. Such an approach contributes to a test year revenue requirement that matches the cost of providing services and, in the Commission's view is fair to both consumers and the utility investors. Nevertheless, the Commission also believes it is appropriate to consider the specific circumstances present in each rate case to determine the appropriate cost of capital. The Commission has reviewed the circumstances present here and while the cases discussed by Ameren and Staff provide useful background, the circumstances are not identical to those present here.

On the one hand, Ameren accuses Staff of intentionally selecting a measurement date that produces an unusually low cost of debt. Staff, on the other hand, accuses Ameren of selective updating to intentionally overstate the cost of capital. The insinuations of Ameren and Staff about the motives or biases of the witnesses are not helpful to the Commission.

Although the Commission favors a consistent period for measuring costs of capital, in this instance Ameren has identified and quantified specific costs of variable

rate debt that increased shortly after Staff's preferred measurement date. Staff does not dispute that the cost of these debt issues increased or assert that Ameren mistakenly reported the current cost of those debt issues. While consistency is important, in this case, fairness requires that the Commission recognize the increased costs faced by CILCO, CIPS, and IP.

Given this situation, the Commission believes it would be appropriate to adjust Staff's embedded cost of debt calculations to reflect the more current cost information associated with the variable rate debt issuances. The Commission has adjusted Staff's embedded cost of debt calculations to reflect Ameren's estimate of the cost of the variable rate debt issues. (Staff Ex. 16.0 at 9-10) The Commission concludes that for purposes of establishing rates in this proceeding it is reasonable to use an embedded cost of long-term debt of 7.08% for CILCO; an embedded cost of long term debt of 6.23% for CIPS; and an embedded cost of long-term debt of 7.04% for IP. Similarly, given the circumstances present in this case, the Commission adopts Ameren's estimate of the cost of short-term debt, 4.96%, for CILCO, CIPS, and IP. The Commission emphasizes that the findings here are not intended to signal a change in policy but, instead, recognize the circumstances present in this specific proceeding.

EXCEPTION 6

VI. Rate Design

C. Cost of Service Issues

1. Minimum Distribution System Study

g. Commission Conclusion

The arguments of IIEC and Wal-Mart have ~~do not~~ persuaded the Commission to direct Ameren, at its option, to prepare and present a cost of service study in the next proceeding incorporating the MDS concept or to furnish the parties to that proceeding with the results of an MDS or zero intercept study. This will allow the Commission to fully consider this approach in future cases without committing the Commission to any particular conclusion about the results of such a study and its use for cost allocation purposes. The Commission recognizes that there are strong theoretical arguments on either side of the MDS issue. It also recognizes that well accepted authorities such as the NARUC Manual suggests this approach and even though the manual is of a 1992 vintage, there has been no change in the function of the utility's distribution system since 1992. Therefore, while the manual does not compel the use of the MDS concept in this case, it certainly justifies consideration of the MDS concept, after the Commission can see the results of studies incorporating the methodology in a future case. ~~deviate from its past decisions and now embrace the MDS. The MDS method fails to properly emphasize the purpose of the distribution system – that being to satisfy a customer's daily demand for electricity. Ameren's method, on the other hand, does not suffer from this weakness. The Commission also continues to believe that distinguishing the cost of connecting customers to the distribution system and the cost of serving its demand remains problematic. Moreover, the Commission is hesitant to rely on the 1992 NARUC manual cited by IIEC and Wal-Mart because of its age and the changes in the electric industry. Accordingly, the Commission will not adopt the MDS in this proceeding.[1] The Commission also declines to adopt IIEC's suggestion that Ameren be required to present a COSS in its next rate case incorporating the MDS approach. In the Commission's view, it would be unreasonable to require Ameren to perform a COSS that incorporates a method repeatedly rejected by the Commission.~~

[1] From the record, it is not clear to the Commission that altering the Ameren COSS to reflect MDS, as Wal-Mart suggests, is even feasible in this proceeding.

EXCEPTION 7

VI. Rate Design

C. Cost of Service

2. COSS Allocation Factor

d. Commission Conclusion

The arguments on both sides of this issue are thought provoking. Traditionally, the Commission has used the NCP demand allocation method in electric cases, based at least in part on the premise that the distribution system is sized to serve maximum demand, whenever that may occur. At the same time, the Commission has recognized in natural gas proceedings that the distribution system serves customer demand every hour of the year and reflected this fact through the use of the A&P demand allocation method. Now, at a time of continuing transition in the electric industry, the Commission is asked to apply the A&P demand method to the electric industry.

Ameren and IIEC seek the continued use of the NCP demand method. The Commission notes that there is evidence in the record which demonstrates the demand related distribution costs represent costs that are essentially the same no matter how many kilowatthours are sold or delivered. These costs are associated with facilties necessary to supply a customer's service requirement at the peak of power consumption. The Ameren Companies' demand related distribution facilities are designed and constructed to be based primarily on local maximum customer loads or demands. These local or maximum loads consist of individual customer or groups of individual customers' loads delivered through a particular distribution line and are tied to the individual customer peak load or the local peak load of the group of customers. As a result, class non-coincident peaks and individual customers' maximum demands are normally used to allocate distribution demand-related plant. Ameren aggregated the components of the distribution plant that were demand related into their various voltage levels and the allocation factors at these voltage levels are based on load research data for class non-coincident peak.

The record here also demonstrates that the NCP method has been traditionally used by Ameren for the allocation of demand-related distribution costs and that the Commission accepted the use of the NCP method in the most recent Commonwealth Edison delivery service case in lieu of the A&P method recommended by the parties in that case.

The record here also demonstrates that CUB is the primary proponent of the A&P method in this case and the arguments and presentations made by CUB are greatly similar to the arguments presented and made by CUB and the other proponents of the A&P method in the ComEd case. Furthermore, the record in this case in support of the NCP method is probably stronger than the record in the ComEd case.

Furthermore, the Commission notes that the record demonstrates there are differences between the gas industry and the electric utility industry that could justify use of the NCP allocator for demand related distribution costs. Furthermore, as IIEC pointed out, in the recent Nicor gas case, Docket 04-0779, the Commission was called upon to evaluate the coincident peak methodology in comparison to the A&P method. IIEC has pointed that there were differences between the coincident peak and non-coincident peak methodology. The non-coincident methodology, according to IIEC, is more granular and does not focus on the demand of all classes at a single hour of the year, whether it focuses on the maximum demands of customers and groups of customers throughout the year regardless of when they occur. The Commission agrees with IIEC that the fact that electricity cannot be stored like natural gas makes it essential to allocate electric distribution costs on the basis that appropriately reflects the timing of the usage. In the case of electricity distribution, the NCP appropriately reflects this timing.

Furthermore, the Commission notes that customer impacts have been a major theme of this case. It would be inappropriate to adopt the A&P method as proposed by CUB given the inaccuracies of the CUB analysis and the fact that the Commission is unable to determine the impact of switching from a methodology that has been in continuous for electric industry in Illinois.

Also, the Commission notes, as IIEC has suggested, that the A&P method as proposed by CUB double counts peak demand. CUB has not explained why double counting peak demand justifies or supports emphasis on average demand.

Finally, the Commission recognizes that the A&P method as proposed by CUB allocates a substantial portion of the fixed costs of the electric distribution system on the basis of electric energy usage and that neither CUB nor any other party has provided any evidence to support the idea that energy usage has any effect on the cost of the distribution system. Indeed, taking CUB's logic one step further suggests that annual usage/energy usage would not occur if there were no customers on the system. Taking CUB's logic to its extreme, one could justify allocation of the distribution system on the basis of the number of customers served, since the distribution system would obviously not have been built if there were no customers to take electric service. In any event, the Commission believes based on the record in this case, that departure from the long established non-coincident peak methodology is not warranted in this case. As we said in the ComEd case, a better developed record may warrant reconsideration of this issue in a future proceeding.

~~Differences in the ability to store the commodities and the period over which peak demand is measured (day versus hour) are among the arguments for the continued use of different demand allocators for the gas and electric industries. Although the Commission agrees that these differences exist, the record in this proceeding does not adequately explain how they justify the continued use of the NCP demand method for the electric industry to the exclusion of the A&P demand method. In the absence of a~~

~~clearer record, the Commission is not persuaded that these differences alone justify the use of different allocators for these industries.~~

~~The Commission is also not as concerned by CUB's faulty impact analysis of the A&P demand method as is Ameren. While knowing the approximate impact of a different allocation method can be valuable, it is not absolutely necessary. Generally, the Commission is aware that use of the A&P demand method will distribute more costs to nonresidential customers than does the NCP demand method.[2] What is puzzling to the Commission is why Ameren is so concerned about not knowing the impact of the A&P demand method on nonresidential customers. Under either demand allocation method, CILCO, CIPS, and IP will recover the same revenue (if done correctly). In any event, CUB's faulty analysis is moot because the revenue requirements approved in these dockets are different from those advocated by the various parties.~~

~~Nor is Ameren's "double-counting" criticism of the A&P demand method persuasive since CUB has explained why more emphasis on average demand is more appropriate. As with gas utilities, an electric utility can not justify its transmission and distribution investment on demands for a single day, much less a single hour, out of a year. The A&P demand method also more equitably reflects the relatively higher usage of residential customers during peak demand, as CUB suggests.~~

~~As suggested was possible in Docket No. 05-0597, a more thoroughly developed record has persuaded the Commission to adopt the A&P demand method in an electric delivery service rate case. Tradition without a record more supportive of the NCP demand method is not enough to justify the continued use of the NCP demand method. Although not a factor in this decision, the Commission notes that use of the A&P demand method will have the overall effect of decreasing costs to residential customers, who have no alternative supplier options, and increasing costs to nonresidential customers, who have alternative supplier options.~~

[2] This fact helps explain why IIEC opposes use of the A&P demand method.

EXCEPTION 8
FIRST ALTERNATIVE

VI. Rate Design

C. Cost of Service

4. Interclass Subsidization

g. Commission Conclusion

A brief word on Ameren's presentation of its rate increase proposal is in order before addressing the interclass subsidization issues. The Commission recognizes that comparing the proposed rates to current bundled and current unbundled rates produces noticeably different results. The Commission also appreciates the need for any rate comparison to be meaningful to customers. Because there are no residential customers taking unbundled service, the Commission understands why a comparison to bundled residential service rates would seem appropriate. Bundled service rates, however, reflect energy costs as well as delivery costs, rendering any comparison with the proposed unbundled residential delivery service rates difficult. Accordingly, the Commission finds that the proper comparison of Ameren's proposed unbundled delivery service rates is to Ameren's existing unbundled delivery service rates. The fact that no residential customers take unbundled delivery service is unfortunate. Nevertheless, Ameren currently has unbundled delivery service rates and these are the rates at issue in this proceeding.

Turning to interclass subsidies, the Commission notes that current delivery service rates are based on cost of service. There do not appear to be any subsidies built into those rates at this time. In the Post 2006 initiative, the parties suggested that delivery service rates be based upon cost and the Commission sees no reason to change that policy at this time. The Commission also notes that it has implemented in the context of the Ameren Companies' power procurement case, a rate mitigation program for residential (DS-1) customers as proposed by the Staff. (Central Illinois Light Company d/b/a AmerenCILCO, et al., ICC Dkts. 05-0160, 05-0161 and 05-0162 (Consolidated), Order, January 24, 2006 at 244-245). In addition, Ameren has voluntarily agreed to a rate cap for residentials in this proceeding and filed in ICC Dkt. 06-0488. The Commission believes the steps taken to date, and those that will be implemented in the future in the pending proceeding, will help to mitigate the impact of any electricity cost increase for residential customers. There is no need to introduce rate subsidies into delivery service rates where none currently exist. Therefore, the Commission directs that the Company use the results of its embedded cost of service study to allocate the rate increase among the customers classes in this proceeding without creating any inter-Class subsidies.

~~Turning to interclass subsidies, the Commission is asked to resolve three issues: 1) whether the demand charge for DS-3 and DS-4 customers should be the same, 2)~~

~~whether CILCO DS-2 rates should increase by 4.51% or 13.02%, and 3) whether DS-4 customers should join DS-2 and DS-3 customers in subsidizing DS-1 customers. With regard to the first issue, the Commission sees some merit to the concerns raised by Kroger if indeed the cost of serving DS-3 and DS-4 customers at the same voltage is essentially the same. Absent any justification, artificial distinctions are generally to be avoided. But more importantly, the Commission wonders if there is sufficient justification for separate DS-3 and DS-4 classes at all. If separate DS-3 and DS-4 classes are appropriate, perhaps the cut-off between the classes is not at the proper demand level. Such questions need not be answered at this time, however, since the Commission lacks sufficient information upon which to make an informed judgment. As with the need for subclasses within DS-3 (as discussed in Section VI. B.), the Commission will defer further consideration of these issues until Ameren's next delivery services rate case. Ameren should address these questions in its next delivery services rate case filing. Until then, the Commission declines to adopt the same distribution delivery charge for DS-3 and DS-4 customers. The resolution of other issues in this proceeding should ameliorate some of Kroger's concerns.~~

~~The second issue stems from Staff's concern over the rate shock that CILCO's DS-2 customers may experience under Ameren's proposed rates. Staff seeks to reduce the impact of the rate increase on CILCO's DS-2 customers by recovering some costs from CILCO's DS-3 customers instead. If this change is made, however, Ameren is concerned about the rate shock that CILCO's DS-3 customers would experience. Rate shock is a legitimate concern and a valid reason for modifying rates. In this instance, the Commission is asked to reduce the rate shock of one customer class at the expense of another. Exactly why CILCO's DS-2 customers should receive such a benefit has not been made clear by Staff. In light of this and the concerns raised by Kroger regarding the DS-3 class, the Commission declines to accept Staff's recommendation regarding CILCO's DS-2 rates.~~

~~As for the third issue, the Commission thoroughly considered the arguments for and against DS-4 customers assisting DS-2 and DS-3 customers subsidize DS-1 customers. While generally it is true that the cost of service should be the guide in setting a customer class' rates, as noted above, the mitigation of rate shock can be a valid reason for deviating from a COSS. To reduce the rate shock experienced by DS-1 customers, Ameren has proposed that DS-2 and DS-3 customers pay more than their respective cost of service. Given the uncertainties coming in January 2007, the Commission believes that it is appropriate to reduce the rate shock of DS-1 customers. The Commission also believes that at least until Ameren's next delivery services rate case that DS-4 customers should share the burden of DS-2 and DS-3 customers in subsidizing DS-1 customers. The Commission has not been convinced by the parties' arguments that DS-4 customers should be treated differently. Including DS-4 will also reduce the burden on DS-2 and DS-3. Accordingly, the Commission adopts Staff's proposal to include the DS-4 class in the contribution to DS-1 rate relief. Additionally, if not already the case, the Commission concludes that it is also reasonable for DS-4 rates to increase by at least 5% in light of the increases experienced by the other customer classes.~~

EXCEPTION 8
SECOND ALTERNATIVE

VI. Rate Design

C. Cost of Service

4. Interclass Subsidization

g. Commission Conclusion

A brief word on Ameren's presentation of its rate increase proposal is in order before addressing the interclass subsidization issues. The Commission recognizes that comparing the proposed rates to current bundled and current unbundled rates produces noticeably different results. The Commission also appreciates the need for any rate comparison to be meaningful to customers. Because there are no residential customers taking unbundled service, the Commission understands why a comparison to bundled residential service rates would seem appropriate. Bundled service rates, however, reflect energy costs as well as delivery costs, rendering any comparison with the proposed unbundled residential delivery service rates difficult. Accordingly, the Commission finds that the proper comparison of Ameren's proposed unbundled delivery service rates is to Ameren's existing unbundled delivery service rates. The fact that no residential customers take unbundled delivery service is unfortunate. Nevertheless, Ameren currently has unbundled delivery service rates and these are the rates at issue in this proceeding.

Turning to interclass subsidies, the Commission is asked to resolve three issues: 1) whether the demand charge for DS-3 and DS-4 customers should be the same, 2) whether CILCO DS-2 rates should increase by 4.51% or 13.02%, and 3) whether DS-4 customers should join DS-2 and DS-3 customers in subsidizing DS-1 customers. With regard to the first issue, the Commission sees some merit to the concerns raised by Kroger if indeed the cost of serving DS-3 and DS-4 customers at the same voltage is essentially the same. Absent any justification, artificial distinctions are generally to be avoided. But more importantly, the Commission wonders if there is sufficient justification for separate DS-3 and DS-4 classes at all. If separate DS-3 and DS-4 classes are appropriate, perhaps the cut-off between the classes is not at the proper demand level. Such questions need not be answered at this time, however, since the Commission lacks sufficient information upon which to make an informed judgment. As with the need for subclasses within DS-3 (as discussed in Section VI. B.), the Commission will defer further consideration of these issues until Ameren's next delivery services rate case. Ameren should address these questions in its next delivery services rate case filing. Until then, the Commission declines to adopt the same distribution delivery charge for DS-3 and DS-4 customers. The resolution of other issues in this proceeding should ameliorate some of Kroger's concerns.

The second issue stems from Staff's concern over the rate shock that CILCO's DS-2 customers may experience under Ameren's proposed rates. Staff seeks to reduce the impact of the rate increase on CILCO's DS-2 customers by recovering some costs from CILCO's DS-3 customers instead. If this change is made, however, Ameren is concerned about the rate shock that CILCO's DS-3 customers would experience. Rate shock is a legitimate concern and a valid reason for modifying rates. In this instance, the Commission is asked to reduce the rate shock of one customer class at the expense of another. Exactly why CILCO's DS-2 customers should receive such a benefit has not been made clear by Staff. In light of this and the concerns raised by Kroger regarding the DS-3 class, the Commission declines to accept Staff's recommendation regarding CILCO's DS-2 rates.

As for the third issue, the Commission thoroughly considered the arguments for and against DS-4 customers assisting DS-2 and DS-3 customers subsidize DS-1 customers. While generally it is true that the cost of service should be the guide in setting a customer class' rates, as noted above, the mitigation of rate shock can be a valid reason for deviating from a COSS. To reduce the rate shock experienced by DS-1 customers, Ameren has proposed that DS-2 and DS-3 customers pay more than their respective cost of service. Given the uncertainties coming in January 2007, the Commission believes that it is appropriate to reduce the rate shock of DS-1 customers. The Commission recognizes that the Ameren Companies excluded DS-4 customers from the "average rebundled" revenue allocation methodology since these customers' delivery service rate contribution as a percentage of their total bill was so much smaller than it was for other rate classes. Including DS-4 customers in the calculation would have produced rates greatly in excess of costs for these customers. Ameren has presented testimony that in some cases increases to DS-4 customers would be from four to seven times the average increase, based on Ameren's revenue request.

IIEC has presented testimony indicating that in some instances, DS-4 customers in the AmerenIP service territory will see a 230% increase in delivery service rates if they simply receive a revenue allocation based on their cost of service. Furthermore, no party has presented any evidence explaining to the Commission or Ameren exactly how to implement the proposal that DS-4 customers contribute to the subsidy. In the absence of such testimony, and considering the obvious adverse rate impacts associated with this proposal, the Commission must reject the proposal to require DS-4 customers to share in the subsidy to DS-1 customers. As noted above, the Commission is again being asked to reduce rate shock for these classes at the expense of another class that may be subject to even greater rate shock. The Commission refused to do so in its resolution of the second issue above and it refuses to do so in this instance.

~~The Commission also believes that at least until Ameren's next delivery services rate case that DS-4 customers should share the burden of DS-2 and DS-3 customers in subsidizing DS-1 customers. The Commission has not been convinced by the parties' arguments that DS-4 customers should be treated differently. Including DS-4 will also reduce the burden on DS-2 and DS-3. Accordingly, the Commission adopts Staff's proposal to include the DS-4 class in the contribution to DS-1 rate relief. Additionally, if~~

~~not already the case, the Commission concludes that it is also reasonable for DS-4 rates to increase by at least 5% in light of the increases experienced by the other customer classes.~~

EXCEPTION 9

VI. Rate Design

A. Summary of Uncontested and Settled Issues

11. Loss Multipliers

Loss multipliers or distribution loss adjustment factors are factors used by a utility to estimate the energy which is lost on the utility's system during transportation to the individual customer. Ameren proposes to change its current practice of separate and fixed multipliers and instead use variable distribution loss multipliers. The proposed loss multipliers are based upon quadratic equations that use the hourly system load as the independent variable. Ameren will then apply the calculations to the customers' energy usage each hour for the combined Ameren Illinois system. While Staff does not contest Ameren on this issue, Staff agrees with many of the observations made by IIEC; in particular that theoretically Ameren's proposal could be more accurate than past practices, but is also more complex. IIEC proposed, and Ameren agreed, that Ameren be required to provide projections of hourly system load figures on its website on at least a day-ahead basis and that Ameren calculate and post the projected distribution loss factors for each voltage class at the same time it posted the projected system loads on the website. The Commission agrees that Ameren should provide the subject information and approves of Ameren's use of variable distribution loss multipliers for the purposes of this proceeding.

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