ILLINOIS COMMERCE COMMISSION

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

REBUTTAL TESTIMONY ON REHEARING

OF

RONALD D. STAFFORD

Submitted On Behalf

Of

CENTRAL ILLINOIS LIGHT COMPANY d/b/a AmerenCILCO,

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

ILLINOIS POWER COMPANY d/b/a AmerenIP

February 28, 2007

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OF

RONALD D. STAFFORD

Q. Please state your name and business address.

A. My name is Ronald D. Stafford. My business address is One Ameren Plaza, 1901 Chouteau Avenue, St. Louis, Missouri, 63103.

Q. Are you the same Ronald D. Stafford who submitted testimony in these proceedings?

A. Yes I am.

Q. What is the purpose of your rebuttal testimony on rehearing?

A. My rebuttal testimony responds to certain issues and recommendations raised by Staff witnesses Burma Jones, Theresa Ebrey, and Peter Lazare. In doing so, I will, among other things, (1) summarize substantiated increases in A&G expenses with which Staff has not taken issue, (2) present the Ameren Illinois Utilities' requested level of A&G expenses, and (3) conclude my testimony with a summarization of the substantiated net increase in A&G expense since the prior delivery service rate cases.

Substantiated Increases in A&G Not Addressed in Staff Testimony

Q. Please identity substantiated increases in A&G expenses with which Staff has not taken issue in direct testimony on rehearing.

A. Shown below is a summary of the substantiated increases in A&G expenses documented on Respondents' Exhibit 53.1 that have not been addressed by Staff in its direct testimony on rehearing:

$11.425 million Depreciation of Ameren Service Assets (Resp. 53.1, Sch. 1, line 6)

$10.321 million Franchise Fees (Resp. 53.1, Sch. 1, line 7)

$(8.022) million Ameren IP A&G Acquisition Cost Savings (Resp. 53.1, Sch. 1, ln. 9)

$5.590 million Salary and Wage Increases (Resp. 53.1, Sch. 1, line 10)

$4.834 million Human Resources and Info. Technology (Resp. 53.1, Sch. 1, line 11)

$1.200 million Ameren Services Interest and Taxes in A&G (Resp. 53.1, Sch. 1, ln 12)

$.733 million Post September 11, 2001 Security (Resp. 53.1, Sch. 1, line 13)

$.589 million Sarbannes-Oxley Compliance (Resp. 53.1, Sch. 1, line 14)

Q. What is the total amount of undisputed increases in A&G expense included above?

A. $26.67 million.

Q. Are pension and benefit expenses included in the above totals?

A. No. The correct amount of 2005 actual pensions and benefits expenses is still at issue. The Ameren Illinois Utilities and Staff are in agreement that the Commission concluded in its November 21 Order that pension and benefits expense should be based on 2005 actual expense. Upon further review, the Ameren Illinois Utilities also agree with Staff that the amount included in the Order is incorrect. Staff's calculation, however, is materially incorrect. Therefore, the parties are not currently in agreement with regard to 2005 actual pensions and benefits expense.

Requested Level of A&G Expenses

Q. Please present the Ameren Illinois Utilities' requested level of A&G expenses.

A. As shown on Respondent Exhibit 55.1, Schedule 1, requested A&G expenses are $36.164 million for AmerenCILCO, $46.089 million for AmerenCIPS, $68.258 million for

AmerenIP. In total, the Ameren Illinois Utilities, the requested level of A&G expenses is $150.511 million. These amounts are slightly lower than the level presented in my direct testimony on rehearing, due to use of surrebuttal rather than rebuttal amounts, in response to the recommendation of Ms. Ebrey.

Response to Staff witness Burma Jones

Substantiation of A&G Expenses

Q. At lines 53-59 and again at lines 62-68 of her testimony, Ms. Jones criticizes your substantiation of A&G increases as being one-sided and focused almost entirely on increases since the prior case. Please respond.

A. As explained at page 25, lines 562-584 of my direct testimony on rehearing, I conducted what I believe was a comprehensive review of the change in A&G expenses from the prior delivery service rate cases to the current rate case. I set an initial materiality threshold for plus or minus changes of $1 million for the Ameren Illinois Utilities on a combined basis, but lowered the threshold during my review to plus or minus $500,000 change from prior A&G expense to current A&G expense for a cost component or cost category.

My review included looking at the detailed A&G expense account information presented in the prior rate cases, adjustments to A&G expense by the utilities and ultimately by the Commission, in an effort to both understand and discern the types of costs included in A&G expense both at per books and after adjustments. During that review, I identified a number of A&G expenses either on the books or utility-proposed cost of service in prior cases that were not included in the current case. The more material examples (those exceeding $1 million) are identified at lines 577-579 of my testimony. I also interviewed each of the accounting witnesses that sponsored

jurisdictional cost of service, and most pro forma adjustments impacting A&G expense. While both AmerenCILCO and AmerenIP were under different ownerships at the time of their prior rate cases, the primary accounting witnesses for both utilities are still with Ameren currently, and have assisted me in analysis and assessment of not only detailed per-book expense by major/minor, but also pro forma adjustments, Commission decisions on A&G issues, differences in accounting for certain expenses (see for example lines 384-451 of my direct testimony on rehearing), other one-time costs, and amortizations. I also reviewed account 925, injuries and damages, due to its fluctuating nature. I also set out to quantify A&G cost savings from the acquisition of Central Illinois Light Company (CILCO), Illinois Power Company (IP), and Asset Transfer of the former Illinois Union Electric Company (UE) operations into AmerenCIPS. As part of that review, I quantified A&G costs savings from the IP acquisition (Resp. 53.1, Sch. 7), reviewed the Orders approving the acquisitions and asset transfer, and interviewed personnel directly involved with A&G expense determinations in each of these transactions, including Ameren's Manager of Acquisitions, and the primary accounting witness that supported the A&G expense evaluation and testimony in the CILCO acquisition case. With regard to CILCO, I identified A&G cost increases that are included in the category of Depreciation of Ameren Services Assets. I identified A&G savings to be realized at the time of acquisition, but had to also assess whether such costs were included in prior rates. As discussed at lines 513-539 of my direct rehearing testimony, I determined that it was impossible for CILCO A&G savings from the acquisition to be included in costs included in the prior delivery service rate case. This has not been refuted by Staff. At lines 547-

560, I discussed the review conducted surrounding the asset transfer of Illinois-UE and AmerenCIPS.

As discussed in my direct rehearing testimony, I did identify savings in amortization of rate case expense, but the savings did not meet the $500,000 materiality threshold. I also identified savings for a reduced number of regulatory and other filings as a result of the UE and CIPS asset transfer as de minimus, but have now quantified those savings in response to a data request from Staff witness Lazare, and have now included those savings with savings in rate case expense on Respondents' Exhibit 55.1, Schedule 1, line 9, column (d).

Q. Why did you establish an initial materiality threshold?

A. The primary reason was to aid the Commission in its review process in these proceedings. Materiality thresholds are often used with regard to cost components. It did not make practical sense to list all identified plus or minus items. In my judgment, the net effect would be immaterial.

Q. Why did you lower your materiality threshold from $1 million to $500,000?

A. As part of my review, I set out to quantify the impact on A&G expense of both post September 11, 2001, security initiatives and the impact of Sarbanes-Oxley compliance. Both efforts are new since the last delivery services rate cases, and both were identified in Respondents' earlier testimony as reasons why A&G expense had increased since the prior delivery service rate cases. While I expected the A&G expense impact to be greater than $1 million, once I realized the impact was actually less than $1 million, I decided to the lower the + or – threshold to $500,000. I considered it relevant information, and

consequently lowered the threshold to capture these and any other identified + or - cost changes between $500,000 and $1 million.

Q. At lines 59-61 of her testimony, Ms. Jones discusses a downward trend in A&G expenses as reason to question whether some A&G expenses have decreased since the prior delivery service rate cases. Do you identify any other decreases in your original analysis?

A. Yes. As discussed above and in my direct rehearing testimony, I did identify other A&G expenses that had decreased since the prior cases, but those cost decreases did not exceed $500,000 for the Ameren Illinois Utilities. As discussed above, however, I have now modified the A&G acquisition cost savings related to UE/CIPS asset transfer to include both savings resulting from reduced regulatory and other filings, and the portion of rate case expense savings attributable to the combination of the former Illinois-UE and AmerenCIPS rate filings. The category of acquisition cost savings already exceeded $500,000 due to the IP acquisition.

Q. Have you identified any additional categories of expense that have increased or decreased by $500,000 or more, and were not included in your original analysis?

A. Yes. In 2003, Ameren initiated a voluntary retirement program ("VRP") that produced additional savings in A&G expense. The allocable portion of those savings attributable to the Ameren Illinois Utilities exceeds $500,000. Therefore, I have quantified the net savings resulting from the VRP, and have summarized those savings on Respondents' Exhibit 55.1, Schedule 1, line 13 and further detailed the savings on Schedule 4.

Q. Do you have any additional comments regarding the downward trend in A&G expenses discussed by Ms. Jones?

A. Yes. The downward trend Ms. Jones refers to is from Staff witness Ebrey's ICC Staff Exhibit No. 24.0, Schedules 24.1 through 24.3. The purported downward trend Ms. Jones refers to is actually an upward trend for AmerenCILCO (Schedule 24.1), a downward trend for AmerenCIPS (Schedule 24.2), and a downward and then upward movement for AmerenIP (Schedule 24.3). As discussed later in my testimony in response to Staff witness Ebrey, these results are distorted somewhat by the inclusion of Account 926.

Ms. Ebrey's A&G cost trend observation has little meaning with regard to the substantiation of A&G cost increases or decreases from the prior delivery service rate cases, which is the subject of Ms. Jones testimony where she discusses trends. That is because in the case of AmerenCILCO and AmerenCIPS, both utilities owned generation assets in 2000, and A&G expenses were supporting not only electric transmission and distribution business lines, but also the generation business lines. In addition, while AmerenIP did not own generation assets in 2000, nor support a generation business line with A&G expenses, a portion of A&G expenses were disallowed as if AmerenIP owned generation at the time. In all three cases, the effect was a lower level of A&G expense in rates than is implied by Ms. Jones' reference to these A&G cost trend schedules as support for her testimony that other A&G costs have decreased. As a point of reference, the sum of 2000 A&G expenses for the Ameren Illinois Utilities, as shown on Schedules 24.1-24.3, was $147.129 million. This compares with A&G included in prior delivery service rates of $49.497 million (Respondents' Exhibit 53.1, Schedule 1, line 1). The difference is almost $100 million, yet Ms. Jones somehow believes this information is

relevant in her criticism of my substantiation analysis. I believe the numbers speak for themselves.

<u>Duplicate or Unintended Disallowances</u>

Q. At lines 70-107, Ms. Jones uses the term "Disallowance Ordered by the Commission" as a way of responding to your testimony regarding Duplicate or Unintended Disallowances. Is she correct in her conclusions?

A. No. While Ms. Jones is correct that the Commission indicated the $50.3 million A&G disallowance in the November 21 Order was over and above all other adjustments, I do not believe the Commission's intent was to disallow the same expense twice, or disallow an expense that was in a category other than A&G expense in the prior case and is now included in A&G expense. Rather, I understand the Commission is requiring information by which to reweigh its deliberation. Further disallowing the same expense twice would directly impair our opportunity to earn our authorized rates of return. Ms. Jones seems to also have agreed with Respondents' conclusion that the $50.3 million reduction of A&G expenses duplicates certain adjustments by her statement i.e.: "While it may appear that the Commission's $50.3 million reduction of A&G expenses duplicates certain adjustments made elsewhere in the Order . . . ." (ICC Staff Exhibit 23.0, Page 5, lines 77 and 78).

It is interesting to note that the one category of expense ($5.7 million of pensions, OPEBs, and Major Medical expense) Ms. Jones uses as her example is not a duplicate disallowance, but rather more in the category of an unintended disallowance (see lines 96-102 of my direct rehearing testimony) on the part of the Commission. This item is unique from the other duplicate disallowances, in that it represents the only cost category where the expense seemed to be allowed in one section of the November 21 Order and

disallowed in another section. Nevertheless, after giving further consideration to this issue, the Ameren Illinois Utilities have elected to withdraw the $5.7 million add back as a component of the substantiated A&G expense increases. The removal of this adjustment is summarized on Respondents' Exhibit 55.1, Schedule 1, line 8 and the removal can be traced to Schedule 2.

Q. Why have the Ameren Illinois Utilities elected to withdraw the $5.7 million adjustment for Pensions, OPEBs, and Major Medical Expense as a substantiated A&G expense?

A. First, as mentioned above, the adjustment is unique from the others in this category. Second, this adjustment is also the only one expressly referenced by Staff witness Jones, so as a matter of compromise the removal of this adjustment limits the number of issues. Third, use of this adjustment creates some confusion with regard to whether the Commission's intent was to allow pensions and benefits expense based on 2005 actual expense. For purposes of this rebuttal testimony on rehearing, the Ameren Illinois Utilities are willing to agree with Staff that the Commission's intention with regard to these costs was to base them on the 2005 actual, consistent with the AG position, rather than based on the portion previously acknowledged by the Commission as supported, based on testimony of Staff witness Lazare.

<u>Prior A&G Disallowances</u>

Q. At pages 6-8 of her testimony, Ms. Jones states that the Ameren Illinois Utilities have taken an inconsistent position with regard to prior A&G disallowances. Is this correct?

A. Absolutely not. As stated in my direct rehearing testimony, for AmerenCIPS, there were no specific A&G disallowances identified in the Order. Conversely, in Docket Nos. 01-

0465/01-0530/01-0637 for AmerenCILCO and Docket No. 01-0432 for AmerenIP, the level of authorized A&G expenses was understated due to a combination of misclassifications and/or disallowances. This understatement thus incorrectly paints the picture that A&G expense in this case had increased more than the actual cost of service. If there had been A&G disallowances identified in the AmerenCIPS case, it would result in an increase to substantiated A&G expenses, and further support my direct testimony on rehearing. On the other hand, if documentation existed that identified AmerenCIPS use of the labor allocator for A&G expense resulted in an overstatement of A&G expense allocated to the distribution business in the prior case, then I would have documented a decrease in substantiated A&G expense resulting from this item. However, the facts are what they are. No such disallowance was made.

Q. Can you explain why you believe no such disallowance was made in the last AmerenCIPS DST rate case?

A. Yes. AmerenCIPS was under different ownership from both AmerenCILCO and AmerenIP at the time of its last delivery service rate case, and took a different approach to A&G. Even if IP at that time were under the same ownership, the approach for IP would have been different because it didn't own generation assets, and consequently A&G expense was not supporting the generation business line. While both AmerenCIPS and AmerenCILCO still owned generation at the time and could have conceivably compared notes and presented pro forma A&G expense in a comparable manner, they didn't. AmerenCILCO chose to take issue with broad use of the labor allocator, and instead elected to detail A&G expense for each minor and each activity while AmerenCIPS presented data based on information at the FERC major account level.

With the additional detail developed by AmerenCILCO, it elected to directly assign in excess of 20 line items of A&G expense to electric generation operations, and employ a number of different allocators to the remaining line items. In summary, AmerenCILCO employed a combination of direct assignment and various allocators that were considered most accurate to determine the appropriate level of expense assignable to electric delivery service, very similar to the approach approved by the Commission in this proceeding to assign General and Intangible Assets to business lines. The evidence supporting the AmerenIP A&G disallowance as a reason why A&G expenses have increased from prior case levels is even more compelling, because there were no generation assets on the books of the IP at time of the prior DST case.

Setting aside this discussion, and the confusion created on this issue, it is significant that the substantiated A&G disallowances can be (1) directly tied to evidence in the prior cases, (2) quantified and measured based on evidence submitted in those cases, and (3) directly identified from a simple review of the Appendix to the Orders, for substantially all of the dollars. There is no reason for the Commission in this case to ignore overwhelming evidence presented by Respondents' to the existence of these disallowances as support for the substantiated increase in A&G expenses in the present case.

<u>Response to Staff Witness Theresa Ebrey</u>

Q. Have you reviewed Ms. Ebrey's testimony where she discusses a difference between the A&G expense levels presented by Mr. Adams and the levels included in Respondents' Rebuttal and Surrebuttal testimony in the case in chief?

A. As Ms. Ebrey points out, Mr. Adams' amount of $153.6 million is from Respondents' initial filing. As I understand it, Mr. Adams used the original filed amounts for simplicity of presentation. In my direct testimony on rehearing, I used the rebuttal levels to be consistent with the information shown on the Appendices to the November 21 Order. After reviewing Ms. Ebrey's direct testimony on rehearing, I agree that it is more appropriate to use the surrebuttal amounts to reflect the Ameren Illinois Utilities' current requested levels.

Q. At line 53 of her testimony, Ms. Ebrey indicates that $152.3 million of A&G expense is the Ameren Illinois Utilities' current requested amount. Is she correct?

A. No. The surrebuttal amount of $150.511 million, as shown on Repondents' Exhibit 55.1, Schedule 1, Page 1, line 19, is the requested amount.

Q. Have you reviewed the A&G cost trend analysis presented by Ms. Ebrey on Schedules 24.1, 24.2, and 24.3?

A. Yes.

Q. Do you have any comments regarding this trend analysis?

A. Yes. As discussed in response to Ms. Jones, the data reflects an upward trend for AmerenCILCO (Schedule 24.1), a downward trend for AmerenCIPS (Schedule 24.2), and a downward and then upward trend for AmerenIP (Schedule 24.3). The inclusion of account 926 creates somewhat distorted results. Since the Commission in these proceedings has concluded that 2005 actual expense should be the basis for pensions, OPEBs, and Major Medical expense (also referred to as pensions and benefits expense), I have recalculated Ms. Ebrey's cost trend analysis. The results are shown on Respondents' Exhibit 55.2 include the following modifications to Ms. Ebrey's

calculation, as follows: (a) exclude account 926, where the majority of pension and benefit expenses reside; (b) replace projected 2006 with actual 2006 information; (c) present the distribution percentage share of 2004, 2005, and 2006 costs in order to better demonstrate the correlation between book A&G expenses and the requested amounts in these proceedings; (d) present both combined and separate schedules for the Ameren Illinois Utilities; and (e) compare the distribution share of per-book 2004-2006 A&G expenses, excluding account 926, with Respondents' requested A&G excluding pensions and benefits expenses.

Q. What does the modified cost trend analysis show?

A. The analysis shows different cost trend percentage results, and in some cases results in a flip of a positive vs. a negative percentage on the trend line. More importantly, requested A&G expense excluding pensions and benefits is $95.051 million (Page 1, Column (F), line 26) which compares favorably with the distribution percentage share of per books expense excluding account 926 for each year 2004-2006. For those years, the range is from $99.2 million to $101.4 million.

Q. At lines 89-91, 102-104, 115-117 of her testimony, Ms. Ebrey argues: "Clearly the amount [of A&G expense] approved by the Commission in the November 21 Order is more reflective of actual results of operations than that requested by the Company." Is that statement correct?

A. No, it is not. The statement is not supported by the facts or logic. The numbers speak for themselves, and are not even close for any of the Ameren Illinois Utilities. Using her Schedules 24.1-24.3 as a point of reference, the November 21 Order allowed A&G expense is $22.667 million for AmerenCILCO compared with 2005 and 2006 shown on

Schedule 24.1 of $36.1 million and $29.5 million, respectively. For AmerenCIPS, the November 21 Order allowed A&G expense is $28.054 million, compared with 2005 and 2006 shown on Schedule 24.2 of $41.3 million and $40.1 million, respectively. For AmerenIP, the November 21 Order allowed A&G expense is $41.730 million, compared with 2005 and 2006 shown on Schedule 24.3 of $67.5 million and $68.2 million, respectively. In summary, Ms. Ebrey's statement is patently incorrect.

Q. Beginning at line 118, Ms. Ebrey appears to criticize Respondents' AMS Reallocation Adjustment. Please respond.

A. This section of her testimony is another example of where, presumably unintentionally, Ms. Ebrey has created confusion about something that seemingly was fully understood by parties during the direct case. The testimony implies for example, that use of 2005 information somehow violates section 287.40 of the Minimum Filing Requirements (line 176). While 287.40 indicates that inflationary adjustments are allowed, she states at line 218 that inflation adjustments are not allowed. There is a long line of precedent before this Commission regarding the use of inflation factors, most recently the decision in the ComEd delivery services rate case, to allow a portion of A&G expense to be recovered based on a general inflation rate.

Moreover, all of Ms. Ebrey's testimony on this point is irrelevant with regard to the AMS Reallocation Adjustment. Both Staff and AG personnel assigned to audit AMS costs understood that the costs were based on six months 2005 actual data annualized, rather than based on some other approach. Actual data is what it is. No one but Ms. Ebrey has implied that the adjustment somehow includes inflation. It would be inconsistent, for example, for Ms. Ebrey to attempt to use 2004 recalculated data in lieu

of later known actual data, and at the same time accept use of IP acquisition cost savings at 2006 and 2007 levels, rather than restate to 2004 cost savings levels.

Whether use of 2005 actual information for six months was entirely clear in my direct testimony was not at issue in the direct case, because it is apparent upon review of the pro forma adjustments and related workpapers (referenced by Ms. Ebrey at line 168).

Putting that point aside, however, if Ms. Ebrey actually believes it is reasonable to attempt to reallocate all 2004 costs with an overlay of the IP acquisition, she also presumes that it is somehow more accurate than use of later known actual data. Such a position is illogical. Simply using 2004 actual data with application of different allocations and different employee levels is no longer the actual data.

Also, she does not discuss (or even acknowledge) either the process that would be required to reallocate costs or the assumptions that would have to be used with repositioned AMS personnel and former IP employees transferred to AMS. Only an employee-by-employee analysis could conceivably produce reasonable results, but the results would still be estimates, unlike use of 2005 actual data.

Q. Beginning at line 196, Ms. Ebrey appears to tie a response to Data Request TEE 13.04 to information that she alleges should have been provided in support of Respondents' original pro forma AMS reallocation adjustment. Please respond.

A. If I understand her testimony correctly, Ms. Ebrey is alleging that isolating the costs related to the IP acquisition on all Ameren companies is somehow the same or similar to the steps undertaken by Respondent to develop its pro forma AMS reallocation adjustment, and/or should have been undertaken to support the original pro forma adjustment. First, as an aside, the data request was objectionable and it was so stated. If

Staff had an issue with discovery, it is my understanding that is to be resolved in procedures other than testimony.

Second, there are significant and material differences between the two exercises. The pro forma AMS reallocation adjustment was calculated based on actual information, and reflected the actual results from all changes related to the acquisition, including changes in allocation factors, and movement of personnel from IP to AMS or another affiliate where applicable, and expenses moved from AMS to IP, where applicable. Labor and other costs moving from IP to AMS were measured by Respondents to avoid duplication.

Ms. Ebrey's Data Request TEE 13.04 did not ask for actual data. It instead requested the impacts of the acquisition on *all* affiliates, which requires not only the use of a number of estimates, such as assumptions on how work would have been performed by pre acquisition employees absent the acquisition, but also whether changes in all A&G expense levels for *all* affiliates were impacted by the IP acquisition and to what extent. To develop such a result with precision, Respondents would have to literally isolate all changes, and rerun the accounting system for *all* affiliates as if the IP acquisition hadn't occurred. This exercise is not technically impossible, but could require significant system costs and an estimated 1,000 or more hours to accomplish. In addition, it is far beyond the scope of Respondents' pro forma AMS reallocation adjustment, which again was based on actual information for the Ameren Illinois Utilities reflecting the addition of AmerenIP (and also reflecting the combination of former Illinois -UE into AmerenCIPS).

Q. At lines 232 and 233 of her testimony, Ms. Ebrey states that she believes Ameren is unable to identify the increased AMS costs related to the IP acquisition. Is she correct?

A. No. In response to Data Request TEE 13.04, and further discussed above, the Respondents stated that to take on such an exercise would be extremely time consuming and labor intensive, because the impact would have to be quantified and measured for all Ameren companies receiving AMS services. Even if such an exercise were undertaken, this one piece of information on its own would not provide a breakthrough conclusion to the reasonableness of AMS costs on a whole, given Staff's overall theme in this testimony.

Q. Do you agree with Ms. Ebrey's conclusion that 2005 actual Employee Pensions and Benefits Expense are incorrect, based upon what was provided by Respondents and included in the Order?

A. Yes. Upon further review it has been determined that 2005 actual expense, as reported, did not reflect actual expense for all cost components. More specifically, the AMS portion of such costs was based on budgeted allocation percentages, and the amounts transferred to construction were also based on budgeted percentages.

Q. At lines 343, 354, and 364, Ms. Ebrey seems to imply that amounts "Transferred to Construction" were not properly accounted for in the determination of 2005 actual pensions and benefits expense reflected in the November 21 Order. Is this correct?

A. No. The fact is that pensions and benefits expenses exclude cost amounts that are "Transferred to Construction" and the accounting was proper.

Q. At lines 340-342, 351-353, and 361-363, Ms. Ebrey makes a similar point, and a more serious allegation, with her alleged double counting of AMS benefit and pension expenses, based on the assumption that those expenses were double counted, by being included in the AMS reallocation adjustment. Please respond.

A. This allegation is made three times in her testimony. She accuses Respondents of doing something improper. In the AMS Reallocation Adjustment, she refers to workpapers at line 168 of her testimony. Those workpapers clearly identify the removal of pension and benefit expenses from accounts 920 and 926. Pensions and benefits expenses related to the Ameren Illinois Utilities' share of AMS costs follow how labor is recorded, and therefore reside primarily in account 920. Respondents elected to exclude these costs from the AMS reallocation, which is clearly identified, and instead include such costs in the pro forma adjustment for pension and benefits expense. These amounts were also included in the 2005 expense which served as the basis for the Commission's November 21 Order, although those amounts were based on allocation percentages rather than actual numbers, which has been corrected, as discussed further below.

Q. At lines 345-346, Ms. Ebrey indicates a lack of understanding of what is meant by the amount of $19.076 million for "IP purchase accounting." What does this cost represent?

A. This costs represents the elimination of purchase, or push-back accounting, as required for ratemaking in the Order issued approving the IP acquisition in Docket No. 04-0294, under Condition Number 13. The adjustment to remove purchase accounting was made as an initial pro forma adjustment. Similarly, in arriving at 2005 expense used for the November 21 Order, purchase accounting was also excluded. Failing to exclude

purchase accounting now, as Ms. Ebrey has done under her calculation, would be in direct violation of the acquisition order.

Q. Please summarize your review of Ms. Ebrey's recalculation of 2005 actual expense.

A. Her overall approach has merit, but as discussed above, she overlooks some critical adjustments that must be made to properly correct expense included in the November 21 Order. Attached is the corrected recalculation of 2005 pensions and benefits expense identified as Respondents' Exhibit 55.3. This recalculation should be used as the basis for the Commission's allowed level of pension and benefits expense on rehearing.

Q. Please describe the adjustments you have made to Ms. Ebrey's recalculation.

A. The first five adjustments are to remove expenses in account 926 that were not individually adjusted by the Ameren Illinois Utilities in its original filings. They are: (1) Employee assistance program expense; (2) Service award program expense; (3) Health screening expense; (4) Education expense; and (5) Ameren Journal expense. While these expenses are 2005 actual, they were not removed in the original pro forma adjustment. Therefore, to include these amounts now would be double counting. The next two adjustments are to add back to the account 926 expense amounts the portion of AMS pension and benefit costs recorded to account 920 (discussed above). The final adjustment is to eliminate purchase accounting for AmerenIP (also discussed above).

Response to Staff Witness Peter Lazare

Q. At lines 326-328 of his testimony, Mr. Lazare calculates that over $90 million of Respondents' $152.3 million is related to AMS, and calls into question the basis for such a large number. Is this a valid concern?

A. No. Virtually all pensions, OPEBs, and Major Medical expenses flow through AMS. The Commission determined in its November 21 Order that these expenses should be based on 2005 actual information. As shown on Respondents' Exhibit 55.2, Schedule 1, Page 1, line 25, these expenses total $55.46 million based on 2005 actual expense. Just this one category of expenses accounts for well over half of Mr. Lazare's $90 million amount referenced. In addition, it should be noted that Respondents' requested level of A&G expense is $150.511 million, consistent with its surrebuttal testimony, rather than the $152.3 million number quoted by Mr. Lazare.

Q. Beginning at line 330, Mr. Lazare raises a concern with regard to whether the Ameren Illinois Utilities have sufficient independence to protect the interest of ratepayers. Please respond.

A. As stated in response to the data request referenced by Mr. Lazare at lines 338-351, requests for service can come from an AmerenCIPS or any other Ameren affiliate. The fact is that the initiation of the service request into the Ameren system is a superior process to what Mr. Lazare seems to be alluding to, because it helps to assure consistency in set-up, and it results in better controls surrounding the service request process. I would expect Mr. Lazare would be interested in a process that generates better controls, given his comments later in testimony regarding the Internal Audit process. Also, it should be noted that if AmerenCIPS needs a service request to be set up, the service may apply to more than one affiliate, such as AmerenCILCO and AmerenIP. To have the same or similar service request initiated into the service request system by more than one employee is not efficient, and weakens controls and consistency. In summary, the process used by Ameren to initiate service requests is the most efficient and consistent

approach, and provides controls surrounding the service request process that aid the reviews conducted by Internal Audit from time to time.

Q. Please respond to Mr. Lazare's comments that distinctly lacking in your presentation of substantiated A&G expense increases/decreases (from prior levels) is any documentation of savings realized by AmerenCIPS and AmerenCILCO from mergers over the years.

A. I devoted a number of pages in my direct testimony on rehearing, and in my earlier rebuttal testimony, to the review of prior delivery service rate Orders issued for all the Ameren Illinois Utilities, along with the Orders issued approving the mergers/acquisitions and asset transfers that have taken place since the prior delivery service rate cases[1]. As Mr. Lazare may have overlooked, it is critical in my analysis to understand whether any A&G savings to be realized are in rates in the prior DST rate cases.

Q. Beginning at line 379, Mr. Lazare discusses the 1995 merger between UE and CIPS. Is this relevant to your analysis substantiating increases/decreases in A&G expense from prior levels included in prior delivery service rates?

A. No. As stated by Mr. Lazare, the merger took place in 1997. Personnel reductions, and economies of scale related to purchasing and other economies (which would impact A&G to some extent) were put in place in 1998. By the 1999 test year used for the prior AmerenCIPS rate case, material savings would have been already pulled out of the business. In addition, a large portion of the A&G expense savings quoted by Mr. Lazare support electric generation, electric transmission, and gas business lines. In the last

[1] Page 16, Line 361 through Page 25, Line 584 of my direct rehearing testimony discuss analysis conducted to understand what costs were in prior DST rates and what net savings, if any, were realized from the various mergers and asset transfer since the prior cases.

delivery service rate case, only about 34% of electric A&G expenses, irrespective of the gas portion, were allocated to the distribution function.

Notably Mr. Lazare also does not even discuss what portion of A&G savings were associated with avoided costs resulting from the merger, such as implementing new systems on a combined vs. separate basis, addressing increased regulatory requirements, and other external influences[2] on a combined rather than a separate basis. These types of savings would of course not be in prior delivery service rates, because they were avoided.

In summary, a large portion of the savings in A&G quoted by Mr. Lazare supported business lines other than electric delivery service. In addition, the A&G savings realized from the 1997 merger were substantially or entirely realized prior to the 1999 rate case, and therefore were not in rates in the prior DST case. A&G savings would also have been realized from avoided costs, which would not have been in rates in the prior DST case. As a result, the merger is not relevant to my analysis substantiating the change in A&G expense from the prior rate cases.

Q. Mr. Lazare attempts to correlate a data request response (lines 401-423) to the entire discussion of the 1997 UE/CIPS merger. How is this relevant?

A. Simply put, it isn't relevant. As explained above, savings were realized prior to the last delivery services rate case; they wouldn't have any bearing on the present case. In responding to Mr. Lazare's data request, I responded to the CIPS/UE merger that produced savings since the prior rate case. That CIPS/UE merger was the UE/CIPS asset transfer that occurred since the prior Ameren CIPS and Illinois-UE rate cases.

Q. Have you reflected the A&G savings result from the asset transfer in your rebuttal exhibits?

[2] Examples would include Post September 11, 2001 Security initiatives and Sarbanes-Oxley compliance.

A. Yes. Respondents' Exhibit 55.1, Schedule 1, Page 1, line 9, column (d) shows net savings of $174,000 resulting from the asset transfer. These savings are further detailed on Schedule 3 of that exhibit.

Q. Why were these savings not included in your original exhibit 53.1 where you substantiated the increase in A&G expense since the prior DST rate cases?

A. As I explained at lines 553-560 in my direct testimony on rehearing, savings resulting from reducing regulatory and other filings were not deemed to be material, and were not quantified at the time of filing my testimony. They have since been quantified, and represent $14,000 of the $174,000 in net savings resulting from the asset transfer. The remaining $160,000 in net savings results from reduced amortization of rate case. I had previously analyzed the category of changes in rate case expense independent of acquisition/merger related savings (lines 580-584). The fluctuation in that category of expense did not meet my materiality threshold of $500,000, and therefore was not included on Respondents' Exhibit 53.1. I agree with Mr. Lazare that the portion of such savings resulting from combined CIPS/UE vs. two separate rate case filings should be included in the category of Acquisition Cost Savings. Due to the IP acquisition, that category of savings already exceeds $500,000. Therefore, these savings are now reflected on my Respondents' Exhibit 55.1.

Q. Do you have any comments regarding Mr. Lazare's testimony at lines 439-445?

A. Yes. Mr. Lazare states here that A&G is the primary area of savings, yet at line 392 he previously indicated only about a third of the savings would be realized from A&G. His testimony is inconsistent on this point. As discussed above, savings realized from the

CIPS/UE merger are already reflected in prior rates, and are not relevant in the present case.

Q. Have you reviewed Mr. Lazare's discussion regarding savings resulting from the merger of CILCO at lines 447-492 of his testimony?

A. Yes.

Q. Do you agree with Mr. Lazare's conclusion at line 450 that the impact of such merger savings would only begin to appear in the current proceeding?

A. Yes. From a ratemaking standpoint that's correct.

Q. Do you have any comments regarding the quoted testimony of an Ameren witness in the CILCO merger case, at lines 455-471?

A. Yes. The Ameren witness, Mr. Craig Nelson, discussed the fact that savings would be sufficient to obviate the need for any near term rate relief, consistent with the rate stabilization proposal.

Q. Has AmerenCILCO violated terms of the rate stabilization proposal by requesting a rate increase at this time?

A. No. New rates in this case went into effect in 2007, which is within the terms of the rate stabilization proposal.

Q. Is the current request for rate relief inconsistent with the statement that savings "will be sufficient to obviate any near term need for rate relief"?

A. No. New rates in this case went into effect in 2007, which is five years since the submission of Mr. Nelson's testimony in Docket No. 02-0428. In addition, no new gas rate cases have been filed since the merger, which further supports Mr. Nelson's testimony on this point.

Q. Do you have any further comments regarding Mr. Lazare's testimony addressing A&G savings from the CILCO merger?

A. Yes. As explained in response to Data Request PL-10.03, the electric distribution share of A&G savings in 2005 was approximately $7.5 million. Also, as explained in response to Data Request PL-10.15 and discussed further at lines 491-496 and 515-517 of my direct rehearing testimony, additional expenditures were required, most significantly in the area of Information Technology (estimated at $13.6 million at time of acquisition). Depreciation of actual Information Technology assets installed to support AmerenCILCO are recorded in an A&G expense account, and impact the level of A&G expense requested in these proceedings, as discussed in more detail in my direct rehearing testimony referenced above.

Q. Back at lines 367-370 of his testimony, Mr. Lazare directs much of his criticism to measurement of CILCO merger savings on your Respondent Exhibit 53.1. Can you reconcile this criticism with your discussion above regarding CILCO merger related costs and savings?

A. Yes. As I discussed at some length in my direct rehearing testimony, and repeated earlier in this testimony, Respondent Exhibit 53.1 (now updated and labeled Respondent Exhibit 55.1) substantiates material increases in A&G expenses in rates from *the* prior case to the current case. For any of the above savings numbers to be relevant for inclusion on that exhibit, the costs that give rise to the merger savings have to be in rates approved in the prior DST rate cases. Otherwise, the savings are not part of the explanation for changes in A&G expense in prior rates compared with Respondents' current requested levels.

The above is true for each of the Ameren Illinois Utilities, but it is particularly on point for AmerenCILCO, whose prior test year was based on an historical level of expense far below years before and after the test year, and well below levels just prior to submission of testimony in support of the merger. For example, A&G labor expense, which is typically the largest area of A&G savings in a merger, was virtually non existent in prior approved rates (see line 535 of my direct rehearing testimony).

Q. At lines 494-507 of his testimony, Mr. Lazare concludes his discussion of the CIPS and CILCO mergers. Please respond.

A. That discussion simply ignores the facts in this case. The facts are that AMS costs make up over 60% of A&G costs in the present rate cases. AMS costs impacting A&G expense in this case are based on May-October 2005 annualized data, except for pensions, OPEBs, and Major Medical expenses, which are based on 2005 actual expense per the November 21 Order. A&G savings in AMS costs realized by May 2005-October 2005 are reflected in Respondents' proposed surrebuttal level of A&G expense. In addition, A&G costs incurred to integrate systems, improve processes, comply with increasing regulatory requirements and external factors realized by May-October 2005 are also in the surrebuttal level of A&G expense.

Q. At lines 565-570 of his testimony, Mr. Lazare draws some conclusions about the internal audit process. Is his concern valid?

A. No. To my knowledge, Ameren's internal audits or internal audit process have not been criticized by the Commission, Staff, or other interested parties as lacking or incomplete, absent Mr. Lazare's comment here. I am not aware that Mr. Lazare has undertaken any review of the audit itself, or inquired about the review process undertaken.

Q. How many hours did it take to conduct the internal audit for Service Request Billing attached to Mr. Lazare's testimony?

A. We estimate, based on conversations with Ameren's Manager of Internal Audit responsible for conducting this audit, that it took about 250 hours to complete the audit that Mr. Lazare discusses. The Manager of Internal Audit has also estimated that the recommendation made by Ms. Jones at lines 186-188 of her testimony would significantly increase the numbers of hours spent on this audit, if adopted by the Commission.

Q. Beginning at line 572 of his testimony, Mr. Lazare expresses concern about the proposed level A&G expenses as it relates to pension and health care benefits pertaining to retired employees. Is his concern valid?

A. No. As indicated in response to a number of data requests from Mr. Lazare, the Commission approved agreements to spin off the generation assets for each of the Ameren Illinois Utilities. These spin off agreements were conducted pursuant to Section 16-111 (g) of the Public Utilities Act concerning the proposed sale of generating plants. The approved agreements contemplated that all pension and health care assets and liabilities related to retirees would be retained by the Ameren Illinois Utilities.

Q. Mr. Lazare complains that the responses to data requests requesting information on pension and health care benefits pertaining to retired employees were vague. Is he correct?

A. No. The Ameren Illinois Utilities provided the requested information. Staff did not contact Respondents after submission of the responses to indicate that either the questions weren't answered, nor did Staff send any follow-up requests to obtain more information.

Q. Mr. Lazare also complains that the responses to data requests estimated health care and pension costs. Is this correct?

A. No. The amounts provided were not estimates. The responses indicated the amounts are not determinable and cannot be estimated. However, the Respondents developed a reasonable allocation, in order to comply with the requests, based upon use of broad assumptions to assess the magnitude of retiree share of such costs, and in turn the production retiree share of the retiree share of such costs. Accordingly, Mr. Lazare's complaint is groundless.

Q. Mr. Lazare also complains that the responses to Data Requests did not provide any accompanying explanation or workpapers. It this a valid complaint?

A. No. Mr. Lazare in his requests asked for amounts. Explanations were also provided. Workpapers were not requested. Thus, the Ameren Illinois Utilities provided the requested information. Based upon the fact that pension and health care costs assets are not maintained separately for active vs. retired employees, and retired employees are not flagged as to whether they retired in production role per se, Respondents provided reasonable responses to the underlying requests.

Q. Can you provide some additional explanation regarding why it is appropriate, under these circumstances, to include these costs for recovery in rates?

A. Yes. First of all, the Commission encouraged spin-off of generation assets as part of the deregulation process. The underlying agreements were structured to put delivery service customers in the same overall position as if the transfer had not occurred, consistent with the provisions of Section 16-111 (g) of the Public Utilities Act.

Second, the active years of service for the since retired employees were on behalf of the Ameren Illinois Utilities and customers served by the Ameren Illinois Utilities during the years of active employment., not on behalf of the newly established company.

Third, the allocation of pension and OPEB benefits in an acquisition or divestiture situation is complex given that the actual cost of those benefits is not known until each plan participant has received his or her last pension payment or the last retiree health care claim has been paid.

Fourth, it is reasonable for ratepayers to be responsible for shortfalls or benefit from surpluses resulting from pension and OPEB benefits that are promised to retirees that worked their entire career for a regulated utility.

Fifth, since the actual cost of those benefits is not known until each plan participant has received his or her last pension payment or the last retiree health care claim has been paid, the costs or gains from the group of production retirees would have been allocated to ratepayers if the spin-off of generation had not occurred.

Sixth, if the pension plan, for example, had a significant surplus of assets at the time the production group was spun off, then spinning off liabilities and assets for production retirees would have required a portion of the surplus assets, funded by ratepayers, to be transferred to the new non regulated production company.

Seventh, even if the plan had a shortfall and assets and liabilities were spun off for production retirees and all those retirees deceased shortly thereafter, then the resulting plans for the active production employees would benefit from a surplus of assets that should have otherwise been used to offset future ratepayer costs.

Q. Do you believe Mr. Lazare would endorse the sixth or seventh option outlined above?

A. I doubt that he would endorse such an option, although he is quick to point towards Respondents' allocation approach to endorse an approach that he perceives takes costs the other direction. As indicated above, it is impossible to know precisely how assets and liabilities associated with retirees would have differed if the plans had been split originally.

Q. Do you have any additional comments regarding why it is appropriate, under these circumstances, to include these costs for recovery in rates?

A. Yes. To the extend there are unfunded costs, which cannot be determined absent an allocation, such costs represent retiree (production and non-production) legacy costs during years of service performed on behalf of the regulated utility, to the benefit of ratepayers. Also, it should be noted that when assets were spun off for the legacy liabilities for active production employees, assets less than liabilities were transferred to the non regulated generation company. The cost for this unfunded liability is not being borne by delivery service ratepayers, but by the new generation company. This cost was incurred during the years that these production employees were working for a regulated utility. In summary, it would be inconsistent to "cherry pick" and reduce the cost of service for an allocated share of production retirees without making a parallel adjustment in the opposite direction for the legacy liabilities of active production employees.

Q. Is Mr. Lazare correct when he says that ratepayers did not receive any remuneration for the spin-off of generation? Please comment.

A. His contention is not relevant in determining whether the utilities should be able to recover these costs. Ratepayers had no property interest in the undepreciated portions of the plants, and were entitled to no compensation. Second, the transfers were encouraged by the General Assembly as part of electric restructuring and authorized by the Commission. There was no requirement for any remuneration to ratepayers, only that the rate freeze and service not be threatened. Neither was threatened, and after the transfers, customers continued to enjoy the benefits of the rate freeze.

Q. If the Commission elects to functionalize a portion of pensions and/or OPEBs expense to production, as Mr. Lazare has suggested, what additional considerations must the Commission make in its determinations of cost recovery in this case?

A. If such costs are functionalized to production, they should be recoverable from power supply customers of the Ameren Illinois Utilities through the Supply Procurement Adjustment provision of Rider MV. The express language in the SPA states in relevant part: "This adjustment shall also include all costs including capital and operating costs for generation resources incurred outside of the CPA process and any costs assigned to the power supply administration function in the Company's delivery service rate cases, as approved by the Commission from time to time."

<u>Reporting Requirements</u>

Q. Did Staff witness Jones make any recommendations regarding reporting requirements?

A. Yes, she suggests the following reporting requirements with the intended purpose of scrutinizing AMS charges to the Ameren Illinois Utilities:

- An annual audit report by AMS Internal Audit Department
- An annual evaluation report of the Service Request policies

- A report identifying the specifics of the bench marking plan
- A report documenting the specifics of the customer review process
- An annual report documenting all customer reviews
- A quarterly report documenting cost/billing challenges
- A report on the internal control analysis

Q. What comments do the Ameren Illinois Utilities have regarding this recommendation?

A. While the Ameren Illinois Utilities do not oppose the reporting requirements, the intent or objective of filing the reports should be further explained. The Ameren Illinois Utilities file a number of reports containing information on topics which are subsequently litigated in rate proceedings. Historically, the Ameren Illinois Utilities have received little to no feedback on the contents of such reports. The Ameren Illinois Utilities are willing to cooperate with the Staff in this regard, but how this data can or will be used continues to be unclear.

Q. Under what scenario would the recommended reporting requirements be reasonable?

A. If the Staff of the Commission routinely reviews the reports, provides comments regarding areas of concern based upon the contents of such reports within a reasonable period of time, and signs off on the reasonableness of such costs, thereby eliminating the potential of re-litigating the cost issues in the next rate proceeding, then the reporting requirements would serve a purpose. Clearly, any costs associated with the preparation of such reports would be directly assigned to the Ameren Illinois Utilities.

Q. Do the Ameren Illinois Utilities substantially agree with the recommendation?

A. For the most part. In the spirit of compromise the Ameren Illinois Utilities are willing to provide the reports except that which calls for the specifics of the bench marking plan. By agreeing to provide these reports, I am not suggesting that the current processes are in any way deficient. Both Mr. Adams and I have explained throughout the legitimacy of the AMS charges and described the protocols in place that ensure the integrity of the AMS charging progress. For example, currently on a biennial basis, an evaluation report of the Service Request policies is provided the Staff. I am not aware that the Staff has taken issue with the contents and conclusions reached in the report in prior years. Note that the creation of this particular report takes approximately 250 hours. Obviously creating the report on an annual basis will mean doubling the hours to be expended, and doubling the expense to our customers. Nonetheless, the Ameren Illinois Utilities will provide the information and reports as described if the Commission believes it will be valuable..

Q. You have indicated opposition to proving the specifics of a bench marking plan. Please explain why that is the case?

A. First, the requested report is vague in terms of scope and direction. It is not clear if all or some of the AMS services are to be bench marked, as one example. Mr. Adams previously offered testimony, unrebutted, explaining how certain of the services offered by AMS really do not exist in the market place or are otherwise so industry specific that bench marking would be impractical. Further, Mr. Adams also testified to the current state of bench marking and I am not aware that Staff has taken specific issue with those processes. It is not clear as to what is intended in terms of timing, that is, a plan that

reviews current bench marking practices, later bench marking efforts, a proposal to develop new bench marking practices, and so forth.

Summary of Substantiated Increases In A&G Expense

Q. Please summarize the substantiated increases in A&G expenses you have supported in your rebuttal rehearing testimony.

A. Respondents' Exhibit 55.1, Schedule 1. Page 1 summarizes the substantiated increase in A&G expenses compared to prior authorized levels. The total amount of substantiated increase in A&G expense is $105.663 million, as shown on line 16. Included in this total is $51.681 million of Pensions and Benefits expense (Resp. 55.1, Sch. 1, line 4).

Conclusion

Q. Does this conclude your surrebuttal rehearing testimony?

A. Yes, it does.