

**STATE OF ILLINOIS  
ILLINOIS COMMERCE COMMISSION**

|   |   |                                 |
|---|---|---------------------------------|
| CENTRAL ILLINOIS LIGHT COMPANY d/b/a AmerenCILCO,         | ) |                                 |
|   | ) |                                 |
|   | ) | Docket No. 06-0070              |
| Proposed general increase in rates for delivery service.  | ) |                                 |
|   | ) |                                 |
| CENTRAL ILLINOIS PUBLIC SERVICE COMPANY d/b/a AmerenCIPS, | ) |                                 |
|   | ) |                                 |
|   | ) | Docket No. 06-0071              |
| Proposed general increase in rates for delivery service.  | ) |                                 |
|   | ) |                                 |
| ILLINOIS POWER COMPANY d/b/a AmerenIP,                    | ) |                                 |
|   | ) |                                 |
| Proposed general increase in rates for delivery service.  | ) | Docket No. 06-0072<br>(consol.) |
|   | ) |                                 |

**AMEREN ILLINOIS UTILITIES' INITIAL BRIEF ON REHEARING**

**March 23, 2007**

|  |    |
|--|----|
| INTRODUCTION .....   | 3  |
| I. Uncontested and Substantiated Issues .....  | 5  |
| A. Pensions and Benefits Expenses .....  | 5  |
| B. Undisputed Issues .....   | 5  |
| 1. Depreciation of Ameren Service Assets .....                                       | 7  |
| 2. Franchise Fees.....   | 8  |
| 3. Ameren IP A&G Acquisition Cost Savings.....                                       | 9  |
| 4. Salary and Wage Increases .....   | 9  |
| 5. Human Resources and Information Technology .....                                  | 9  |
| 6. Ameren Services Interest and Taxes in A&G.....                                    | 10 |
| 7. Post September 11, 2001 Security .....  | 11 |
| 8. Sarbanes-Oxley Compliance.....  | 12 |
| 9. Maintenance of General Plant.....   | 13 |
| 10. Incentive Compensation.....  | 13 |
| 11. Parent Company Payroll Distribution.....   | 14 |
| C. Duplicate Disallowances.....  | 14 |
| 1. Injuries and Damages.....   | 15 |
| 2. Incentive Compensation.....   | 16 |
| 3. Amortization of Procurement Case Expense .....                                    | 16 |
| II. Comparison of Test-year Expenses to Previously Authorized A&G levels.....        | 17 |
| A. Prior A&G Disallowances .....   | 19 |
| 1. AmerenCILCO – A&G Expense Allocator .....   | 19 |
| 2. AmerenIP .....  | 21 |
| B. Other (All Utilities).....  | 22 |
| III. Pensions and Benefits Expenses .....  | 24 |
| IV. AMS Service Charges Are Reasonable .....   | 28 |
| A. AMS Allocation Methods .....  | 34 |
| B. Benchmarking of the Ameren Illinois Utilities’ A&G Costs to Other Utilities ..... | 40 |
| V. Market Studies .....  | 42 |
| VI. Implementing Rate Changes .....  | 50 |
| CONCLUSION.....  | 51 |

## INTRODUCTION

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, (collectively, the “Ameren Illinois Utilities”), hereby submit this Initial Brief on Rehearing. Respectfully, and in short, the Commission’s November 21, 2006, Order in this case did not allow the Ameren Illinois Utilities to be able to recover their prudently incurred costs and earn a reasonable rate of return on their investments, as Illinois law requires the Commission to do. The law is unambiguous on this point: “In setting rates, the Commission must determine that the rates accurately reflect the cost of service delivery and must allow the utility to recover costs prudently and reasonably incurred.” *Citizens Utility Board v. ICC*, 166 Ill. 2d 111, 121 (1995); *see also* 220 ILCS 5/1-102(a)(iv), 9-201(c), 16-108(c). Moreover, the Commission must base such a determination on the record evidence in a litigated proceeding – and on nothing else.

No other party but Staff presented testimony on rehearing, and the large majority of the Ameren Illinois Utilities’ direct evidence was undisputed by Staff testimony. As shown on Respondents’ 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’ requested level of A&G expenses is \$150.511 million. The rehearing evidence thus shows a necessary total increase of \$105.663 in the Ameren Illinois Utilities’ Administrative and General (“A&G”) expenses compared to prior authorized levels, as follows:

- As a preliminary matter, the Ameren Illinois Utilities presented *undisputed* rehearing testimony showing that they are entitled to recover \$26.67 million over previously approved A&G expense amounts. As no party presented evidence to dispute recovery of those amounts, the utilities’ entitlement to that recovery could not be clearer.

- The Ameren Illinois Utilities also demonstrated that prior A&G disallowances explain \$24.818 million of the increase in A&G expense in this proceeding. Of this total, Staff did not address the \$1.609 million portion unrelated to the A&G expense allocator.
- The Ameren Illinois Utilities also demonstrated \$9.433 million in duplicate disallowances in the November 21, 2006 Order. After addressing issues raised by Staff, \$3.410 million (Resp. Exh. 55.1, Sch. 1, p. 1, line 8), of these apparent errors were not directly disputed by Staff or any other party.
- The utilities also demonstrated an *appropriate* comparison of A&G expense increases to prior DST levels, based on actual demonstrated costs and *not* on an outdated methodology that is not useful to test-year ratemaking and inapplicable to the record evidence in this case.
- Further, the Ameren Illinois Utilities have shown the reasonableness of their A&G costs in comparison to other utilities, as requested in the Commission’s December 21, 2006, rehearing order, by providing the following (largely undisputed) evidence:
  - an analysis of the services provided by Ameren Services Company to all Ameren companies,
  - details on how those costs are fairly allocated among the companies,
  - the results of a study showing the costs of services obtained from Ameren Services Company and comparing those costs with market costs.

Thus, based on the evidence presented in this rehearing proceeding, the Commission should conclude that the Ameren Illinois Utilities’ A&G expenses are reasonable, fully substantiated and must be recovered under law.

## **I. UNCONTESTED AND SUBSTANTIATED ISSUES**

### **A. Pensions and Benefits Expenses**

The Ameren Illinois Utilities and Staff are in agreement that the Commission's November 21 Order indicated that pensions and benefits (also referred to as pensions, OPEBs, and Major Medical) expenses should be based on 2005 actual information (Order p. 78).

The Ameren Illinois Utilities and Staff are also in agreement that the Commission's November 21 Order does not reflect actual 2005 pensions and benefits expenses (ICC Staff Exh. 24.0, p. 17, Respondents' Exh. 55.0, p. 17).

In calculating actual 2005 pension and benefits expenses, the Ameren Illinois Utilities and Staff are also in agreement that purchase accounting should be excluded. At hearing and in a subsequent filing, Staff corrected an error in Ms. Ebrey's direct testimony, where she failed to exclude purchase accounting for AmerenIP as required by the Commission's Order approving the IP acquisition in Docket No. 04-0294, Condition Number 13. (Tr. p. 178, lines 11-22; p. 179, lines 1-9; Staff Ex. 24.0 Corrected, lines 345-346 & Schedule 24.10; *see also* Resp. Ex. 55.0, pp. 18-19.) Staff's correction of this error results in a \$19.076 million upward adjustment to Staff's direct testimony level of electric pensions and benefits expenses, prior to delivery services allocation, for AmerenIP. (Staff Ex. 24.0 Corrected, Schedule 24.10.)

In addition, Ameren Illinois Utilities now agree with Staff that smaller program expenses are only counted once under Staff's approach to use account 926 as a starting point in calculating 2005 actual pensions and benefits expense, and no further adjustment is necessary.

### **B. Undisputed Issues**

The chart below shows each of the categories for which *no* party presented testimony in dispute of the Ameren Illinois Utilities evidence, and the corresponding appropriate adjustment to A&G expense (in millions):

|   |                 |
|---|-----------------|
| Depreciation of Ameren Service Assets<br>(Resp. 53.1, Sch. 1, line 6)                           | \$11.425        |
| Franchise Fees<br>(Resp. 53.1, Sch. 1, line 7)  | \$10.321        |
| Ameren IP A&G Acquisition Cost Savings<br>(Resp. 53.1, Sch. 1, ln. 9)                           | \$(8.022)       |
| Salary and Wage Increases<br>(Resp. 53.1, Sch. 1, line 10)                                      | \$5.590         |
| Human Resources and Information<br>Technology (Resp. 53.1, Sch. 1, line 11)                     | \$4.834         |
| Ameren Services Interest and Taxes in<br>A&G (Resp. 53.1, Sch. 1, line 12)                      | \$1.200         |
| Post September 11, 2001 Security<br>(Resp. 53.1, Sch. 1, line 13)                               | \$.733          |
| Sarbanes-Oxley Compliance<br>(Resp. 53.1, Sch. 1, line 14)                                      | \$.589          |
| Prior A&G Disallowance -<br>Maintenance of General Plant<br>(Resp. 53.1, Sch. 3, line 3)        | \$.677          |
| Prior A&G Disallowance -<br>Incentive Compensation<br>(Resp. 53.1, Sch. 3, line 5)              | \$.462          |
| Prior A&G Disallowance -<br>Parent Company Payroll Distribution<br>(Resp. 53.1, Sch. 3, line 6) | \$.470          |
| Duplicate Disallowance –<br>Injuries and Damages<br>(Resp. 53.1, Sch. 6, lines 1 and 2)         | \$1.050         |
| Duplicate Disallowance –<br>Incentive Compensation<br>(Resp. 53.1, Sch. 6, line 3)              | \$1.466         |
| Duplicate Disallowance –<br>Amortization of Procurement Expense<br>(Resp. 53.1, Sch. 6, line 4) | \$.894          |
| <b>Total Undisputed A&amp;G Increase</b>  | <b>\$31.689</b> |

The Ameren Illinois Utilities' undisputed evidence supporting these individual categories is discussed briefly below.

## **1. Depreciation of Ameren Service Assets**

Depreciation of Ameren Services Company (“Ameren Services” or “AMS”) Assets is one explanation for why A&G expenses have increased in the present proceeding.

(Respondents’ Exhibit 53.0, pp. 21-22; Exhibit 53.1, Schedule 1, line 6.) While the rebuttal level of A&G expense attributable to depreciation expense of AMS assets was not at issue in the current proceeding, the Commission’s \$50.3 million disallowance provides for \$0 recovery of this cost of providing service to electric delivery service customers.

Most intangible plant assets installed by Ameren are recorded on the books of the Ameren Services Company, and directly assigned or allocated to the various Ameren Companies who utilize and/or benefit from such systems. Similarly, general plant assets owned by Ameren Services Company also are either direct assigned or allocated to the various Ameren Companies who utilize and/or benefit from such assets. The direct assignment or allocation of such costs is governed by the General Services Agreement approved by the Commission for each of the Ameren Illinois Utilities. Depreciation of these assets is recorded on the books of the Ameren Companies as an expense to Account 923, an A&G account. As such, the increase in depreciation expense attributable to these assets, from the amount allowed in prior orders, represents a quantified, substantiated reason why A&G expense has increased in the present proceeding.

Prior to Ameren’s acquisition of CILCO and IP, intangible and general plant assets were recorded as an asset on the books of these companies, with related depreciation expense recorded as depreciation, rather than A&G expense. In the acquisition of CILCO (Docket No. 02-0428, Ameren Schedule 3.2), it was contemplated that at least \$13.6 million of Information Technology system expenditures would be needed. Approximately one half of AmerenCILCO’s \$5.126 million of depreciation expense shown on Exhibit 53.1, Schedule 1, line 6, column (c) is

attributable to implementation of CILCO into Ameren's customer service system. With regard to IP, a substantial amount of intangible and general plant was retired as part of the conversion of IP to Ameren's systems, and IP is now integrated into Ameren's systems, resulting in a net reduction to authorized utility plant in service and depreciation expense in the present proceeding, and an increase in A&G expense for conversion of IP to Ameren's systems.

Unlike CILCO and IP, AmerenCIPS was on Ameren's systems at the time of its prior order. Therefore, only the net change in such costs from prior authorized levels is reflected on Exhibit 53.1, Schedule 1, Line 6. For each of the Ameren Companies, these undisputed costs are further detailed on Exhibit 53.1, Schedule 4, and total \$11.425 million.

## **2. Franchise Fees**

Unavoidable and necessary franchise fee cost increases give rise to a significant component of increase in A&G expense that was disallowed by the Commission. (Respondents' Exhibit 53.0, p. 3.) Notably, these costs have not been disputed by any party in this case, in either the primary hearing or on rehearing,<sup>1</sup> and such costs were not included as a component of cost of service by the utilities in the prior rate proceedings. Thus, no party's testimony or evidence supports the Commission's disallowance of the cost of franchise payments and free or discounted service to municipalities in which the utilities provide service. Indeed, this disallowance is inappropriate, because such expenses are an undisputable cost of doing business, and because revenues at present rates appropriately reflect the impact of related billing determinants.

---

<sup>1</sup> Only the AG (and only in its direct case), and no other party, disputed the Ameren Companies' adjustment in this case to include this cost for recovery. AG Ex. 1.0, pp.16-18 (AmerenCIPS), AG Ex. 1.0, pp. 19-21 (AmerenCILCO), AG Ex. 1.0, 26-28 (AmerenIP). Notably, the AG accepted the Ameren Illinois Utilities' rebuttal adjustment to include all related billing determinants giving rise to free or discounted service in the calculation of revenues at present rates, in rebuttal testimony. (AG Ex. 3.0, pp. 10-11.)

The Commission should thus allow the substantiated franchise-related costs in allowed A&G expense in the amount of \$10.321 million as detailed on Respondents' Exhibit 53.1, Schedule 5.

### **3. Ameren IP A&G Acquisition Cost Savings**

A total of \$8.022 million of A&G related IP acquisition savings were identified in the current rate proceeding, and reflected in test year expense. (Respondents' Exhibit 53.0, p. 24.) This level of test year savings is reasonably representative of A&G related savings from prior test year levels. Therefore, this amount is reflected as a quantified, substantiated reason why A&G expense has decreased in the present proceeding, from prior authorized levels.

### **4. Salary and Wage Increases**

Due to the passage of time, salaries and wages will necessarily increase due to a combination of cost of living/inflation adjustments, performance, the overall market for similarly priced positions, and negotiation results for union-based rates. (Respondents' Exhibit 53.0, pp. 8-9.) Based on these and other factors, A&G Salaries and Wages included in test year expense, based on 2006 salary and wage levels, are higher today than at the time of the prior test year, which was based on 2000 or 2001 salary levels, depending on the Company. It is reasonable to conclude, therefore, that increases in A&G Salaries and Wages represent a quantified, substantiated reason why A&G expense has increased. An uncontested adjustment to reflect these increased costs is shown on Respondents' Exhibit 53.1, Schedule 8 in the amount of \$5.59 million.

### **5. Human Resources and Information Technology**

Prior to acquisition by Ameren, CILCO did not have either a Human Resources or an Information Technology department at the time of its last rate case. (Respondents' Exhibit 53.0, p. 9.) To the extent that CILCO, at that time, got by with a minimum level of such service, it

outsourced such work. A review of test year employee levels submitted in the prior rate case confirmed this conclusion, in that no test year 2000 employees were identified from either department. An expanded review of FERC reported total electric expense recorded to Account 920, A&G Salaries combined with Account 923, Outside Services, confirmed that the level of service being provided was at a materially low level in the prior test year 2000. For the four years prior to calendar year 2000, average A&G Salaries were \$5.5 million, compared with \$2.1 million in the test year. Similarly, Outside Services averaged about \$3 million, compared with less than \$600,000 in the test year. Therefore, to properly address the understatement of A&G expense at the time of the last test year, at least to the extent it relates to the Human Resources and Information Technology functions, it is necessary to reflect AmerenCILCO's rebuttal level of such costs net of any outside services costs included in the prior test year, as an explanation and justification, for the increase in this A&G expenses in the present case. An uncontested adjustment to reflect these increased costs is shown on Respondents' Exhibit 53.1, Schedule 9 in the amount of \$4.834 million.

#### **6. Ameren Services Interest and Taxes in A&G**

Ameren Services incurs Interest Costs due to its need to obtain funds to pay for services provided, primarily through Money Pool borrowings in advance of reimbursement by the Ameren Illinois Utilities. (Respondents' Exhibit 53.0, pp. 9-10.) Similarly, Ameren Services pays a relatively small amount of income, property, and franchise taxes. Allocation of such costs is governed by the General Services Agreement approved by the Commission for each of the Ameren Illinois Utilities, and the Ameren Illinois Utilities' share of such costs is recorded to Account 923, A&G expense. The uncontested adjustment shown on Respondents' Exhibit 53.1, Schedule 10 represents the net increase in such cost from levels approved in prior orders, in the amount of \$1.2 million.

## **7. Post September 11, 2001 Security**

The Ameren Illinois Utilities have incurred significant additional costs to safeguard assets, systems, and personnel since the events of September 11, 2001. (Respondents' Exhibit 53.0, pp. 10-12.) Ameren has initiated a number of programs and incurred substantial investment to step up and improve security and protect from potential terrorism threats. In many cases, the decision to implement the programs and incur the costs was the result of an increased awareness, from a business perspective, that protection of assets, systems, and personnel was critical to Ameren's ability to operate as a utility service provider in a safe and reliable manner.

The identified A&G expenses cost categories related to Post-September 11, 2001 Security are as follows:

- Relocate Corporate Mail Room
- Infrastructure Disaster Recovery – second Data Center with some duplicate hardware and third party restoration for back-up of critical systems
- Intrusion Detection System and Sensors
- Business Continuity initiatives and planning
- Compliance with Critical Infrastructure Protection and Critical Cyber Assets Committees and other North American Electric Reliability Counsel initiatives
- Additional firewall protection to filter out incoming data from countries with known terrorist activity
- Proxy Server Perimeter Security
- Additional Corporate security employees responsible for breach investigation
- Additional Security Guards at regional facilities
- Card access software and maintenance costs

- Additional personnel to maintain card access system and Closed Circuit TV systems

A&G expenses attributable to the Ameren Illinois Utilities' electric delivery service business have been substantiated for recovery as a cost attributable to this category, as summarized on Respondents' Exhibit 53.1, Schedule 1, line 13 and detailed on Schedule 11. This uncontested electric delivery service share of such costs attributable for the test year totals \$733,000, which is deemed to be an ongoing A&G expense impacting electric delivery services.

## **8. Sarbanes-Oxley Compliance**

The Sarbanes-Oxley ("SOX") Act, implemented in 2002, requires publicly held companies to formally assess internal controls, and the practices and systems for keeping records, with substantial emphasis on prevention of abuse and/or fraud. (Respondents' Exhibit 53.0, pp. 12-13.) Ameren initiated SOX compliance in 2003 and completed the initial phase of such compliance at the beginning of 2005.

SOX Compliance Costs will continue into the foreseeable future, because they represent an improved business practice of assessing processes and controls that benefit all direct and indirect users of financial information, including this Commission. The actual costs from year to year could vary somewhat, but the overall costs will continue. For example, in 2006, SOX costs are somewhat lower than 2005, but are expected to increase in 2007 due to additional Securities and Exchange Commission sector reporting requirements.

The Ameren Illinois Utilities' uncontested electric delivery service share of SOX compliance costs is \$589,000 as shown on Exhibit 53.1, Schedule 1, line 14 and further detailed on Schedule 12.

## **9. Maintenance of General Plant**

In Docket Nos. 01-0465/01-0530/01-0637, account 935 Maintenance of General Plant was presented by the Company as a component of “Maintenance” rather than “A&G” expense (CILCO WPC-1c). (Respondents’ Exhibit 53.0, p. 18.) Therefore, the authorized amount of \$1,043,317 (Staff Exhibit 16.0, Schedule 2) was recorded as Maintenance expense. Since Account 935 is classified as an A&G expense account as reported in the Federal Energy Regulatory Commission (“FERC”) Form 1, AmerenCILCO in the present case reported this expense as A&G. As such, the rebuttal amount of such expense, or \$677,000 as shown on Respondents’ Exhibit 53.1, Schedule 3 also represents a quantified, substantiated reason why A&G expense has increased in the present proceeding.

## **10. Incentive Compensation**

It is appropriate to recognize an adjustment for prior AmerenCILCO incentive compensation expense as an explanation for why A&G expenses have increased in the present proceeding because, in Docket Nos. 01-0465/01-0530/01-0637, all test year incentive compensation expense was reported to an Operations expense account 580. (Respondents’ Exhibit 53.0, p. 19.) However, Staff’s adjustment, adopted by the Commission, to remove incentive compensation expense was incorrectly classified as an adjustment to A&G expense. As such, A&G expense was reduced by \$462,000 (Order, Appendix A, Schedule 7, page 2, col B, line 9), resulting in a negative, rather than \$0 balance in A&G expense attributable to incentive compensation expense. Due to this misclassification, this amount represents a quantified, substantiated reason why A&G expense was understated in the prior Order and in turn directly explains a portion of the A&G increase in the present proceeding. This correction is reflected on Respondents’ Exhibit 53.1, Schedule 3.

## **11. Parent Company Payroll Distribution**

Parent Company Payroll Distribution is also an explanation for why AmerenCILCO's A&G expenses have increased in the present proceeding because, in Docket Nos. 01-0465/01-0530/01-0637, A&G expense was reduced by \$470,000 (Order, Appendix A, Schedule 7, page 2, col B, line 14), for an expense that was not reflected in AmerenCILCO's A&G expense. (Respondents' Exhibit 53.0, p. 19.) In that proceeding, the Company responded to Staff Data Request BAP 7.03 and indicated as follows: "The parent company payroll distribution represents CILCO payroll charged to CILCORP and other non-regulated affiliates and activities." As confirmed in discussions with the accounting witness sponsoring this data request response, the express language of this response was intended to demonstrate that the payroll dollars in question were already removed from Company payroll expense. Therefore, no further adjustment was appropriate. However, the Staff witness in that proceeding, who may have misinterpreted the response, reduced A&G expense by an additional \$470,000. Due to not discovering this error until the time of the hearings, the Company was unsuccessful in getting Staff to reverse this adjustment, and it was adopted by the Commission. As a result, this incorrect A&G disallowance had the effect of creating a negative balance in A&G expense for this expense component in the prior rate order. Correction of this error is reflected on Respondents' Exhibit 53.1, Schedule 3 represents a quantified, substantiated reason why A&G expense has increased in the present proceeding.

### **C. Duplicate Disallowances**

The November 21, 2006 appears to have duplicated disallowances totaling \$9.104 million, detailed below and on Respondents' Exhibit 53.1, Schedule 6. The principal components of the duplicate disallowances are Pensions and Benefits, Injuries and Damages, Incentive Compensation, and Amortization of Procurement Case Expense.

Staff Witness Burma Jones offered no testimony to directly dispute these apparent duplications in disallowance. Rather, Ms. Jones merely characterized the disallowance as a “Disallowance Ordered by the Commission,” while agreeing that “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 70-107). Ms. Jones’ only argument is that the \$50.3 million A&G disallowance in the November 21 Order was over and above all other adjustments. However, there is *no* indication that the Commission intended 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, nor would there be any logical basis for doing so. Further disallowing the same expense twice would directly impair the Ameren Illinois Utilities’ opportunity to earn their authorized rates of return.

The only category of expense (\$5.7 million of pensions, OPEBs, and Major Medical expense) that Ms. Jones directly refuted in testimony was *not* identified as a duplicate disallowance, but, rather, as an apparently unintended disallowance. (Resp. Ex. 53.0, Lines 96-102.) That item represented the only cost category where the expense seemed to be allowed in one section of the November 21 Order and disallowed in another section. Because this adjustment is unique, and the only one that Ms. Jones directly refuted, the Ameren Illinois Utilities removed the adjustment in rebuttal testimony in order to limit the number of issues. (Respondents’ Ex. 55.0 (Revised), lines 179-202.) Thus, there is no evidence to refute each appropriate adjustment for duplicate disallowances.

### **1. Injuries and Damages**

Disallowance of a portion of Injuries and Damages Expense for AmerenCILCO and AmerenCIPS represents a Duplicate Disallowance, because adjustments to the requested rebuttal level of costs for both AmerenCILCO and AmerenCIPS were made by the Commission. These

adjustments were based upon an average of actual claims incurred after the prior test years. In addition, a review of account 925 for both AmerenCILCO and AmerenCIPS indicates that the rebuttal level of such expense for this account has increased by an amount in excess of prior levels. Therefore, the \$1.05 million disallowed portion of this cost shown on Respondents' Exhibit 53.1, Schedule 6 represents a cost increase over prior allowed levels, which has been both individually disallowed by the Commission in this case, and also collectively disallowed as part of the \$50.3 million disallowance.

## **2. Incentive Compensation**

For each of the Ameren Illinois Utilities, Incentive Compensation Expense was a cost specifically disallowed by the Commission in the prior delivery services rate orders. As such, the Ameren Illinois Utilities' requested level of such costs in these cases totaling \$1.466 million shown on Respondents' Exhibit 53.1, Schedule 6 represents a cost increase over prior allowed levels, which has been both individually disallowed by the Commission in this case, and also collectively disallowed as part of the \$50.3 million disallowance.

## **3. Amortization of Procurement Case Expense**

The Commission proceedings giving rise to the Amortization of Procurement Case Expense represents a Duplicate Disallowance, as this expense is new to the Ameren Illinois Utilities as of this case. As such, the Ameren Illinois Utilities' requested level of such costs shown on Respondents' Exhibit 53.1, Schedule 6, or \$894,000, in these cases represents a cost increase over prior allowed levels, which has been both individually disallowed by the Commission in this case, and also collectively disallowed as part of the \$50.3 million disallowance.

## **II. COMPARISON OF TEST-YEAR EXPENSES TO PREVIOUSLY AUTHORIZED A&G LEVELS**

The primary components giving rise to the overall net increase in A&G expenses are shown on Exhibit 55.1, Schedule 1. More specifically, they are summarized into the following categories:

- Pensions and Benefits
- Prior A&G Disallowances
- Depreciation of Ameren Services Assets
- Franchise Fees
- Duplicate disallowances
- Acquisition Cost Savings
- Salary and Wage Increases
- Human Resources and Information Technology costs
- Ameren Services Interest and Taxes in A&G expense
- 2003 Voluntary Retirement Plan
- Post September 11, 2001 Security costs
- Sarbanes-Oxley compliance costs
- Other

The implicit assumption (intended or otherwise) in many parties' arguments and in the Commission's decision is that the Ameren Illinois Utilities have not justified any increase in A&G costs since 1999 or 2000 – the test years employed by the Ameren Companies in their last DST cases, other than pensions, OPEBs, and major medical. This is obviously not correct, and the record evidence indicates overwhelmingly to the contrary. The Ameren Illinois Utilities do not believe that the Commission intended to require on rehearing an item-by-item reconciliation of the changes in A&G costs from the levels approved in the last round of DST cases, but they did so in their rehearing testimony.

Rates in this case are being set on a 2004 test year. A 1999 or 2000 test year has no application here, but that is what the Commission used to determine the appropriateness of two-thirds of A&G expenses. The Ameren Illinois Utilities understand that the Commission concluded that it lacked evidence to do otherwise, and that is what this rehearing phase is intended to address. The Ameren Illinois Utilities have provided the Commission with evidence on which it can conclude that the A&G costs reflected in the test year are reasonable. Staff reasoned its way to a level that is very close to what the Ameren Illinois Utilities proposed, and that was accepted by the Administrative Law Judges in the Proposed Order (Proposed Order, pp. 65-66).

Even if it were proper to rely on a 1999 or 2000 test year, which it is not, it is important to note that the baseline that the Commission derives from those cases is not a proper starting point for determining the appropriate level of A&G. In the original DST cases, the Commission was faced with several different means of allocating costs between distribution and generation functions within the utilities. All of the utilities were then vertically integrated, and none was affiliated with another, meaning that the Commission had at least four simultaneous rate cases on an expedited time schedule. The labor expense allocator was an attractive alternative at the time. It was easy to perform, could be applied quickly, and could be applied uniformly to all electric utilities with DST cases. Moreover, any effects of over- or under-allocating costs were moderated by the application of a transition charge. If the Commission set delivery rates too low, it would be offset by a higher transition charge, and vice versa.

The Ameren Illinois Utilities demonstrated in this case that the labor expense allocator is an extremely unreliable means of allocating both investment and expenses. Changes in labor levels frequently produce counter-intuitive results. It is not the Ameren Illinois Utilities' intent to relitigate the use of the general allocator in the prior case, but the Ameren Illinois Utilities do

not believe that it is appropriate to use it as a baseline. For example, a reduction in force due to greater reliance on a service company, would allocate service company costs away from a utility, not to it. Using the result of a such an allocator as a yardstick to assess the reasonableness of A&G expenses several years down the road is not appropriate, and it is not surprising that a comparison of then to now leads to eye-popping results. This does not mean that the Ameren Illinois Utilities are doing anything inappropriate or unreasonable today – rather, it shows what we have already shown. The labor expense allocator was and still is ill-suited for allocating A&G expenses, and is, at the very least, a very different methodology from looking at actual costs and expenses.

**A. Prior A&G Disallowances**

In both 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 and, in turn, painted a picture that A&G expense in this case had increased more than the actual cost of service. These 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. Simply put, the rehearing evidence on these disallowances directly explains the substantiated increase in A&G expenses in the present case.

**1. AmerenCILCO – A&G Expense Allocator**

In Docket Nos. 01-0465/01-0530/01-0637, the Commission reduced A&G for AmerenCILCO due to a combination of misclassifications and disallowances, which have been aggregated into the prior A&G disallowance category and detailed on Exhibit 53.1, Schedule 3. Specifically, this category includes the following cost at issue with Staff that resulted in an

understatement of the level of A&G expenses allowed in the prior order, and directly impacting the amount of increase in A&G expense requested by the Ameren Illinois Utilities in the present case.

The A&G Expense Allocator disallowance from the prior AmerenCILCO case can be used to justify in part the increase in A&G expenses in the current case because, upon initial review of this adjustment made by Staff and accepted by the Commission in the prior AmerenCILCO rate case, it appeared that this adjustment boiled down to strictly a difference of opinion on which was the appropriate allocator to use for A&G expense. However, upon further review of the AmerenCILCO workpapers, it becomes readily apparent that AmerenCILCO directly assigned costs to a specific business line where possible, and only applied an allocator when a particular cost was associated with more than one business line. More specifically, in excess of 20 line items of A&G expense were assigned 100% to electric generation operations. For the remaining line items of A&G expense, a number of different allocators were employed to assign costs to the various lines of business, based upon the allocator best aligned with the cost in question. The approach that the Commission adopted, however, was based on a purely functional allocation approach employing only one allocator for all unadjusted test year costs, without regard to whether a particular cost even applied to the electric distribution business, or whether certain costs apply to one line of business more than another line of business. Under that approach, each of the costs assigned by the Company 100% to electric generation was assigned 46% to electric distribution. All other test year costs were also assigned 46% to distribution through use of the same allocator, without regard to the nature of any specific cost. Therefore, it is apparent that the A&G Expense Allocator adjustment in the amount of \$3.593 million (Order, Appendix A, Schedule 2, page 4, col DD) is not due to a difference of opinion as to the appropriate allocator to use for a specific cost or costs, or a disallowance or imprudence of

a particular expense, but rather an application of an arbitrary approach to the assignment of such costs.

## **2. AmerenIP**

In Docket No. 01-0432, the Commission reduced A&G for IP by \$19.616 million (Order, Appendix A, page 3, col 1). In the present case, the Commission based its ruling on statements made by Staff, which did not reflect or acknowledge the \$19.616 million prior case disallowance as one of the reasons for an increase in A&G from the prior case, even though such information was presented to Staff as an explanation for the increase in A&G expense in response to Data Requests PL-3.1 and PL-3.2. As discussed below, this disallowance was arbitrary and distinguishable from any assignment of A&G costs in any other IP DST case. And, by taking this prior disallowance into account, a picture is painted of A&G expenses increasing by \$19.616 million more than the actual cost of service. As such, this amount represents a quantified, substantiated reason why A&G expense has increased in the present proceeding.

In the prior AmerenIP delivery services rate case, unlike AmerenCILCO and AmerenCIPS, generation assets had previously been divested. A&G expense was not supporting generation. Even if argument could be made that it was supporting generation, the \$19.616 million disallowance could not and was not traced to any specific A&G expense in that case, but rather relied entirely on a formula that was derived from the first DS case when IP still owned generation. Therefore, since the disallowance does not reflect elimination of any particular expense, this disallowance should be distinguished from any assignment of A&G expenses to the generation business in the AmerenCILCO or AmerenCIPS' cases, and recognized now by the Commission as a legitimate reason why costs in the present case have increased by \$19.616 million.

**B. Other (All Utilities)**

The Ameren Illinois Utilities also presented evidence that, in the prior rate cases, a number of one-time costs or amortizations were identified. (Respondents' Exhibit 53.0, p. 25; Respondents' Ex. 55.0, beginning at p. 6.) For each such cost identified, test year expense levels were adjusted to normalize or amortize the unusual amounts. Additional adjustments were made by the Commission for some items. Three items with an A&G impact in excess of \$1 million were identified (CILCO Voluntary Employee Retirement Program reduction, CIPS deregulation start-up, and IP severance). In all three cases, A&G expense was restated to \$0 by the Company or Commission. In addition, a further review was conducted of amortization of rate case expense and injuries and damages. While there is some fluctuation from Company to Company, the combined + or – impact for the Ameren Companies is not material (combined impact of \$500,000 or greater), and therefore no additional individual adjustments are reflected on Exhibit 53.1.

The acquisition of CILCO in Docket No. 02-0428 resulted in an increase in A&G expense for implementation of CILCO on Ameren's systems. These costs are reflected in the rehearing adjustment for Depreciation of AMS Assets. In addition, certain other costs and savings were identified by Ameren (Company Schedule 3.2 filed in Docket No. 02-0428) to impact CILCO's overall cost of service. A review was conducted of these other identified costs and savings to assess impact on A&G expense. Only the category of labor cost savings required further review for potential A&G impact. A total of 52 net positions were identified for elimination, based on 2001 actual head count. Of this total, only 1 position charged all or a portion of their time to electric A&G expense. From this total, it was determined that less than \$50,000 of A&G expense would be attributable to the electric delivery services business. Since this analysis was conducted based upon 2001 head count, a point in time subsequent to the prior

DST case, a further review was conducted to assess whether test year 2000 unadjusted A&G labor expense was consistent with A&G labor expense that coincided with the acquisition head count review, or in this case electric A&G expense recorded to Account 920 A&G Salaries for 2001 and 2002. This review indicated that 2000 was materially lower, by about \$1.4 million than average 2001 and 2002 data, based upon data reported to FERC. A separate review was conducted of Commission authorized A&G labor expense in the prior order. After application of all labor and labor-related adjustments, including Staff's arbitrary allocation approach to all A&G costs, and other labor-related adjustments for incentive compensation and parent payroll distribution made in error that materially understated A&G labor expense, the Commission allowed level of A&G labor expense was less than \$50,000. As a result of these two independent analyses, it was determined that it would not be appropriate to show a reduction in A&G expense related to labor cost savings for CILCO, since the test year did not coincide with the acquisition review, and based on level of A&G labor included in the DST order in that case.

Finally, with regard to AmerenCIPS, a review of the Order that approved the transfer of the former Illinois jurisdictional Union Electric assets to Ameren CIPS (Docket No. 00-0650) indicated that some A&G savings could be realized through combined regulatory filings. With regard to this category, any savings related to the combined filing of one rate case for AmerenCIPS, rather than two separate filings for CIPS and former Illinois Union Electric operations, is reflected in test year A&G expense through a reduction in rate case expense.

In responding to issues raised by Staff in its Rebuttal Filing, the Ameren Illinois Utilities substantiated additional savings of \$174,000 resulting of the transfer of the former Illinois Union Electric operations into AmerenCIPS and also substantiated savings of \$742,000 resulting from the 2003 Voluntary Retirement Plan. These savings are detailed on Respondents' Exhibit 55.1,

Schedule 3 and Schedule 4, respectively, and are summarized on Respondents' Exhibit 55.1, Schedule 1, line 9, column (d) and Schedule 1, line 13, respectively.

### **III. PENSIONS AND BENEFITS EXPENSES**

The Ameren Illinois Utilities and Staff are in agreement that the Commission's November 21 Order indicated that pensions and benefits (also referred to as pensions, OPEBs, and Major Medical) expenses should be based on 2005 actual information (Order p. 78).

The Ameren Illinois Utilities and Staff are also in agreement that the Commission's November 21 Order does not reflect actual 2005 pensions and benefits expenses (ICC Staff Exh. 24.0, p. 17, Respondents' Exh. 55.0, p. 17). While the amounts included in the Order were based on expenses rather than total costs, in that they reflected elimination of the costs transferred to construction (Tr. 187, Resp. Exh. 55.0, p. 17, lines 385-389), 2005 actual expense included in the Order did not reflect 2005 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 (Resp. Exh. 55.0, p. 17, lines 381-384). In addition, the adjustments adopted by the Commission were primarily based on proposals made by the AG. The AG, however, did not attempt to adjust all pensions and benefits expenses to 2005 actual levels (Order pp. 74-76), although they did endorse use of 2005 actual information (Order p. 78).

In Rehearing, Staff has recommended that 2005 actual expense be based on the amounts shown on FERC Form 1 for Account 926 (ICC Staff Exh. 24.0, Attachments F, G, and H). Respondents agree that use of Account 926 can serve as a reasonable starting point for determining 2005 actual pensions and benefits expense, provided that certain modifications are made. In its Rebuttal Testimony, the modifications proposed by the Ameren Illinois Utilities were: (1) elimination of smaller program expenses not individually adjusted in Respondents' in

its original filings; (2) inclusion of pensions and benefits expenses for the Ameren Illinois Utilities' share of Ameren Services employees recorded to account 920; and (3) elimination of purchase accounting for AmerenIP (Resp. Exh. 55.0, pp. 18-19, Resp. Exh. 55.3).

With regard to item (1) elimination of smaller program expenses, since 2005 actual expenses for these programs are included in account 926, the Ameren Illinois Utilities now agree with Staff that no further adjustment is necessary for this cost category. Elimination of these expenses to avoid double counting would have been appropriate if actual expense was based on Respondents' pro forma adjustment. Since Staff, however, has proposed on Rehearing to use Account 926 as the starting point for such determination, these expenses are only counted once, and require no further adjustment.

With regard to item (3), Staff has revised its calculation of AmerenIP pensions and benefits expense to exclude purchase accounting. Therefore, the Ameren Illinois Utilities and Staff now agree that Account 926 needs to be modified to eliminate purchase accounting (ICC Staff Exh. 24.0, Sch. 24.10 Revised, line 2, line 2, Respondents' Exh. 55.3, Sch. 1, Page 3, line 8).

Therefore, the only modification to the Account 926 balance, as reported on FERC Form 1 for 2005 still at issue is whether the Account 926 balance should be modified to include pensions and benefits expenses for the Ameren Illinois Utilities' share of Ameren Services employees recorded to account 920. Staff bases its exclusion for these costs on the assumption that such costs are double counted in the AMS reallocation adjustment (ICC Staff Exh. 24.0, p. 18, lines 340-342 for AmerenIP, p. 19, lines 351-353 for AmerenCILCO, p. 19, lines 361-363 for AmerenCIPS).

In the Commission's November 21 Order, such amounts were included in pensions and benefits expense, rather than the AMS reallocation adjustment, in determining 2005 actual

expense. Specifically, for AmerenIP, ICC Staff Exh. 24.0, Attachment F identifies \$6,632,073 of AMS employee pensions and benefits expenses included in amounts in data request BCJ 6.14 and recorded in accounts other than account 926 for AmerenIP. For AmerenCILCO, ICC Staff Exh. 24.0, Attachment G identifies \$2,915,744 of AMS employee pensions and benefits expenses included in amounts in data request BCJ 6.10 and recorded in accounts other than account 926. For AmerenCIPS, ICC Staff Exh. 24.0, Attachment H identifies \$5,528,135 of AMS employee pensions and benefits expenses included in amounts in data request BCJ 6.04 and recorded in accounts other than account 926.

In the AMS reallocation adjustment, those workpapers identify the removal of pensions and benefits expenses from Accounts 920 and 926 (Resp. Exh. 55.0, p. 18, lines 396-397). Since amounts recorded to Account 920 have been excluded in the AMS reallocation adjustment, these expenses clearly are not double counted.

ICC Staff Cross Exhibit 3 on Rehearing is a copy of the workpaper in support of Exhibit 55.3 that details 2005 AMS portion of actual pension and benefits expenses recorded to account 920 rather than account 926 (Tr. 71-74). This workpaper also details the annualized six months ended 10/31/05 level of such expense, and actual 2004 expenses eliminated in the AMS reallocation adjustment. Since the AMS reallocation adjustment is based on the difference between May-October 2005 expense annualized and 2004 test year data (ICC Staff Exh. 24.0, p. 9, line 167, Resp. Exh. 55.0, p. 14, line 319), elimination of the AMS portion of pensions and benefits could have been accomplished in either a one-step or a two-step process, producing mathematically the same result. Respondents elected to eliminate the difference from pro forma 2005 levels vs. test year 2004 levels in one step rather than separately eliminate the amounts in each column in two steps. (Tr. 81)

On ICC Staff Cross Exhibit 3 on Rehearing, for AmerenCILCO, annualized six months ended 10/31/05 expense was \$1,668,852 and actual 2004 expense was \$2,744,236 for a difference of \$(1,075,384). This same \$(1,075,384) was eliminated in the AMS reallocation adjustment. (ICC Staff Cross Exhibit 4 on Rehearing column labeled “remove pensions & benefits”, Account 920, Tr. 77-82, Tr. 184-185). As indicated above, Respondents could have separately eliminated from account 920 \$1,668,852 from the annualized six months ended 10/31/05 expense and \$2,744,236 from actual 2004 expense and produced the same mathematical result for account 920 as was accomplished by Respondents in a one-step process (Tr. 81).

On ICC Staff Cross Exhibit 3 on Rehearing, for AmerenCIPS, annualized six months ended 10/31/05 expense was \$2,605,270 and actual 2004 expense was \$3,367,364 for a difference of \$(762,094). This same \$(762,094) was eliminated in the AMS reallocation adjustment. (ICC Staff Cross Exhibit 5 on Rehearing column labeled “remove pensions & benefits”, Account 920, Tr. 83-84, Tr. 184-185).

On ICC Staff Cross Exhibit 3 on Rehearing, for AmerenIP, annualized six months ended 10/31/05 expense was \$7,166,946 and actual 2004 expense was \$0 for a difference of \$7,166,946. This same \$7,166,946 was eliminated in the AMS reallocation adjustment. (ICC Staff Cross Exhibit 6 on Rehearing WPC-2.3.3, Page 2, col. (I), line 70, Tr. 83-84, Tr. 180-185).

In summary, the Ameren Illinois Utilities and Staff agree that actual 2005 pensions and benefits expense from the November 21 Order need to be modified. The parties also agree that FERC Form 1 account 926 should be used as a starting point, and also agree to exclude purchase accounting. The only remaining issue is whether the Ameren Illinois Utilities’ share of pensions and benefits expenses for Ameren Services employees recorded to account 920 should also be included. Staff’s basis for exclusion of such expenses is the presumption that they are also

counted in the AMS reallocation adjustment. As discussed above, these expenses were fully eliminated in the AMS reallocation adjustment and, therefore, have not been double counted, as alleged by Staff.

In its Order on Rehearing, the Commission should set pensions and benefits expenses for the Ameren Illinois Utilities, as follows: For AmerenCILCO, the calculation presented by Staff on ICC Staff Exhibit 24.0, Schedule 24.8 should be adjusted to include the AMS portion of pensions and benefits expenses from lines 6 and 7 of Respondents' Exhibit 55.3, Schedule 1, Page 1. For AmerenCIPS, the calculation presented by Staff on ICC Staff Exhibit 24.0, Schedule 24.9 should be adjusted to include the AMS portion of pensions and benefits expenses from lines 7 and 8 of Respondents' Exhibit 55.3, Schedule 1, Page 2. For AmerenIP, the calculation presented by Staff on ICC Staff Exhibit 24.0, Schedule 24.10 (Revised) should be adjusted to include the AMS portion of pensions and benefits expenses from lines 6 and 7 of Respondents' Exhibit 55.3, Schedule 1, Page 3.

#### **IV. AMS SERVICE CHARGES ARE REASONABLE**

The Ameren Illinois Utilities have demonstrated the reasonableness of Ameren Services Company ("AMS") charges to the Ameren Illinois Utilities, as requested by the Commission in its Final Order in these dockets.

The Commission is concerned about the magnitude of the increase in A&G expenses and the lack of substantiation for these increases. It seems that the increase may be attributable to the Ameren companies' relationship with Ameren Services. However, the record does not contain enough information for the Commission to assess whether the Ameren companies' are being allocated a fair share of the costs of these services for ratemaking purposes or whether the amounts paid to Ameren Services are reasonable for such services. The Commission has the obligation to ensure "just and reasonable" rates but cannot do so if it is unable to determine if the services that the Ameren companies receive through Ameren Services are indeed being provided at the lowest cost. Therefore, the Commission directs the Ameren companies to conduct a study to show the costs of services obtained from Ameren Services and

compare those costs with market costs. Also as part of the study, the Ameren companies shall provide an analysis of the services provided by Ameren Services to all Ameren companies and provide details on how those costs are allocated among the companies. The Ameren companies shall include the result of the study in the next rate filing.

Order at pp. 66-67.

The Ameren Illinois Utilities' A&G costs consist of charges both from Company personnel and from AMS, an Ameren subsidiary that provides its parent and fellow subsidiaries business and corporate services to a number of the Ameren companies. AMS was formed in connection with the merger of Union Electric Company and Central Illinois Public Service Company in the mid-1990s. AMS operates in accordance with a General Services Agreement ("GSA"), which the Commission initially approved in connection with the merger of Union Electric Company and CIPSCO, which owned Central Illinois Public Service Company (now d/b/a AmerenCIPS), in ICC Docket No. 95-0551. The Commission approved adding Central Illinois Light Company d/b/a AmerenCILCO as a party to the GSA in ICC Docket No. 03-0279. Illinois Power Company d/b/a AmerenIP is also a party to the GSA, as approved by Commission order in conjunction with Ameren's acquisition of that utility in ICC Docket No. 04-0294. AMS does not earn a profit on the services that it provides to the Ameren Illinois Utilities. AMS' services are provided at cost.

For the calendar year 2004, approximately 63 percent of AmerenCILCO's A&G charges were attributable to services provided by AMS. Approximately 65 percent of AmerenCIPS' A&G charges were attributable to services provided by AMS for the same 12-month period.

For purposes of the test year in this proceeding, actual allocated billings from AMS for the period May 2005 through October 2005 were used to estimate the cost of AMS services AmerenIP would need for the calendar year. During the actual billing months of May 2005 through October 2005, approximately 61 percent of AmerenIP's A&G expenses were

attributable to services received from AMS. Thus, a significant portion of A&G expenses do not come from AMS, and come directly from other sources. Ameren witness Stafford addresses some of these sources – such as franchise fees – in his testimony. (Respondents’ Ex. 53.0, pp. 3-4.) To the extent that those items have increased in cost, they have nothing to do with the relationship between AMS and the Ameren Illinois Utilities.

Through the testimony of Michael Adams, the Ameren Illinois Utilities have shown that there has been no affiliate abuse and that the Ameren Illinois Utilities’ A&G costs are reasonable. Specifically, Mr. Adams’ testimony demonstrates:

- The trend of overall A&G expense levels for each of the Ameren Illinois Utilities from the calendar year 2000 through 2004 and the test year.
- The nature of the services provided by AMS to the Ameren Illinois Utilities and how such charges are assigned or allocated to the Ameren Illinois Utilities.
- The allocation of AMS charges are performed consistent with the existing GSA.
- The Ameren Illinois Utilities’ A&G expenses compare favorably to other energy companies.
- Recent studies have been performed by AMS to ensure the reasonableness of its costs.

The standards to which the Ameren Illinois Utilities were held by Mr. Adams during his review, in terms of the portion of their A&G costs which were assigned or allocated from AMS, consisted of the following three criteria: (1) Were the services provided by AMS to the Ameren Illinois Utilities necessary to provide service to the Companies’ customers? (2) Were the costs associated with the services reasonable? and (3) Were the costs allocated to the appropriate entities which benefit from such services in a manner consistent with sound cost causation principles? (Respondents’ Ex. 56.0, p. 10, beginning at line 195) If the answer to each of these

questions was affirmative, then the portion of the Ameren Illinois Utilities' A&G expenses which were assigned or allocated to the Ameren Illinois Utilities from AMS were deemed reasonable and should be included in each Companies' revenue requirement and recovered from the Companies' delivery service customers. No other party to these proceedings offered any standard by which to evaluate the reasonableness of AMS' charges.

In fact, based upon the evidence presented by Staff witnesses Ebrey and Lazare, it appears that, absent its own standard, Staff is focused more on justifying the Commission's elimination of the \$50.3 million of A&G expenses than it is on assessing the reasonableness of the Ameren Illinois Utilities' A&G expenses as required by the Commission's Order on Rehearing.

Respondents' Exhibit 54.1 shows the trend in overall A&G expenses for each of the Ameren Illinois Utilities for the calendar years 2000 through 2004, as well as the test year expense levels requested in these proceedings. As the exhibit shows, the book A&G expense levels for two of the three Ameren Illinois Utilities (AmerenCIPS and AmerenIP) have declined since each of the Ameren Illinois Utilities' last delivery service tariff cases. AmerenCILCO's costs have increased, but this is due to the Company's unreasonably and unsustainably low cost level prior to its acquisition by Ameren Corporation ("Ameren"), as discussed by Mr. Ronald Stafford (Respondents' Exhibit 53.0).

The evidence shows that AmerenCILCO's overall A&G expenses increased from \$16.8 million in 2000 to \$61.9 million in 2004. (Respondents' Ex. 54.3) The test year, as filed in AmerenCILCO's direct case, reflected A&G expenses of \$33.3 million. The increase in A&G expenses from 2000 to 2004 was primarily attributable to three accounts; Account 926, Pensions and Benefits plus \$20.0 million, Account 925, Injuries and Damages, plus \$9.7 million and Account 920, A&G salaries, plus \$7.9 million. Respondents' Ex. 54.4 shows the same

information regarding AmerenCIPS' A&G expense levels. As the exhibit shows, AmerenCIPS' overall A&G expenses declined from \$58.7 million in 2000 to \$52.7 million in 2004. The test-year level of expense per the Company's initial filing was \$42.9 million. Increases in Account 926, Pensions and Benefits and Account 925, Injuries and Damages were offset by decreases in Account 923, Outside Services.

AmerenIP's overall A&G expenses declined from \$71.6 million in 2000 to \$49.6 million in 2004. (Respondents' Ex. 54.5) The as-filed test year level of A&G expenses as filed in this proceeding were \$77.4 million. The increase in test-year expenses is associated with increased Pensions and Benefits costs, franchise fees and AMS costs (net of Dynegy costs). These increases were offset by lower injuries and damages costs and acquisition savings, the latter of which was acknowledged by the Commission in its Final Order.

Respondents' Exhibit 56.1 shows the trends in A&G expenses for each of the Ameren Illinois Utilities and the test year level of A&G expenses per the Companies' surrebuttal filing. The exhibit shows that, in total, the overall level of A&G expenses has declined since 2000 and has remained fairly flat from 2001 through 2006. As has been pointed out throughout this proceeding, the parties are comparing the proposed A&G costs in these proceedings, which use a 2004 test year, to the level of costs reflected in each of the Ameren Illinois Utilities' last DST proceedings. Central Illinois Light Company and Illinois Power Company (prior to their acquisitions by Ameren) both used historical calendar year 2000 test years in their last DST proceedings. AmerenCIPS used an historical calendar year 1999 test year in its last DST proceeding. As Mr. Stafford discusses, in those cases, the Commission used a general allocator, based on labor expense levels, to allocate A&G expenses. Thus, the increase certain parties are referring to is not an increase on the books, but rather the difference between costs incurred during the test year and the level produced by application of the allocator.

The Ameren Illinois Utilities do not concede that it was ever appropriate, but it is particularly inappropriate now. The Ameren Illinois Utilities' operations have changed dramatically since the last round of DST proceedings. In the case of AmerenCIPS, the Company divested itself of its generation business in 2000, the year after the test year used in its last DST proceeding. In the case of AmerenCILCO, the Company was acquired by Ameren and divested itself of its generation business. Both CILCO events occurred in 2003, or three years after the test year for its last DST proceeding. In the case of AmerenIP, Ameren acquired only the "pipes and wires" businesses and supporting assets (i.e., no generation business) from Dynegy in 2004. While a labor expense allocator may have been useful at one time in allocating A&G expenses to the different business functions-generation, distribution-and transmission—its use and more importantly its application is purposeless where the utilities no longer own generation and where direct assignment is now available.

Unlike the last DST proceedings where there was a need (or in the case of IP, a perceived need) to determine the amount of A&G costs which should be assigned to each line of business, during the 2004 test year the generation businesses existed in separate companies and were already assigned or allocated their appropriate share of the A&G expenses. In the case of AmerenIP, no generation assets were acquired by Ameren. Hence, there can be no assignment of A&G expenses, which is the implied affect when comparing A&G expense levels from 2000 to 2004.

The appropriate starting point for comparing each of the Ameren Illinois Utilities' levels of A&G expenses in these proceedings is *not* the level which was approved by the Commission in each of the Ameren Illinois Utilities' last DST proceedings. The Commission adopted and approved cost allocation to each of the Ameren Illinois Utilities' lines of business given the specific costs and circumstances existing at that point in time. The evidence shows that each of

the Ameren Illinois Utilities has undergone significant changes since its last DST proceeding. (Respondents' Ex. 54.0, beginning at p. 6, line 140) In the cases of AmerenCILCO and AmerenIP, it would be inappropriate to judge the costs and associated levels of service provided by the former owners of those companies with the costs and levels of services provided by Ameren to the Ameren Illinois Utilities. The uncontroverted direct testimony of Martin J. Lyons shows that the level of support and costs for both of those Companies was insufficient and not sustainable. (AmerenCILCO Ex. 2.0, pp. 8-11; AmerenIP Ex. 2.0, pp. 7-11.)

It is simply not reasonable to conclude that, merely because the overall level of the costs assigned or allocated to the electric distribution businesses of the Ameren Illinois Utilities has increased, the costs themselves are unreasonable. To determine the reasonableness of the costs assigned or allocated to the Ameren Illinois Utilities' electric distribution businesses, it is necessary to review the nature of the specific costs and how those costs were assigned or allocated to the individual Ameren Illinois Utilities.

**A. AMS Allocation Methods**

AMS provides the following types of services to the Ameren companies:

- Accounting services;
- Accounts payable;
- Budgeting;
- Communications;
- Construction;
- Corporate communications;
- Corporate Planning;
- Customer services;
- Engineering;
- Finance;
- Human resources;
- Industrial relations;

- Information technology;
- Legal;
- Procurement; and
- Tax.

All of these services are necessary to ensure a utility company's sustainable operation, reliability, and overall health, and, in many instances, the services that are needed by the utility cannot be readily procured in the market. For example, regulatory services are critical to any utility, such as rate design and tariff interpretation. It is therefore important that the utility retain such services within the company.

In-house legal costs also include attorney counseling and advisory services necessary to a utility's day-to-day operations. Because public utilities law is highly specialized, and there are few practitioners in the markets where the Ameren Illinois Utilities operate, the companies require a well-qualified in-house legal department.

Tax services are another example of services that an affiliated company can provide more competently and efficiently than through outsourcing. Because tax laws and regulations that apply to utilities can be unique, it makes good business sense to have on hand a company like AMS to serve these needs. In addition, the Ameren Illinois Utilities have found it to be more cost-effective and efficient to have these services provided by a shared services company instead of retaining the capabilities within each of the individual companies.

It is common for companies such as AmerenCILCO, AmerenCIPS and AmerenIP to have a shared services organization such as AMS. (Respondents' Ex. 54.0, p. 12, line 251-255) Whenever services are provided to more than one company, it is typically more cost effective to centralize those services into one company and provide such services to the affiliates from one centralized location.

If each Company provided or procured its own services there would be inherent duplications and ineffectiveness associated with the services. AMS allows the utilities to operate more efficiently.

As stated in AMS' Service Request Manual, all activities performed by AMS for Ameren Corporation or one of its subsidiaries must have a completed and approved service request application. Approvals are required by either Ameren Corporation or the Ameren subsidiary requesting the work, the AMS service provider and the AMS Controller's Department. (Staff Cross Exhibit No. 2 on Rehearing.) No AMS charges may be assigned or allocated to the Ameren Illinois Utilities if the companies have not requested the service, agreed to the level of service, and approved the method of allocation. This information is set forth on the service request.

A "service request" is a request that AMS provide one of the services listed in the GSA, to the utility. There is no guarantee or expectation that every service need will be provided by AMS.

Company witness Lyons described the methods by which AMS tracks and records its costs and assigns such costs to the appropriate entity which received the benefit of the service. AMS has developed and implemented such accounting policies, procedures and systems in a manner consistent with the GSA. Costs are accumulated through a centralized service request system. For each service provided or project performed, AMS determines the appropriate service request(s) required to provide for the accumulation of related cost and the proper allocation factors necessary to apportion such cost to the specific Ameren subsidiaries receiving such services or benefiting from such projects. Prior to implementing use of new allocation factors, AMS personnel are required by the SEC to attain written approval through submission of

a letter describing the type of costs to be allocated and the rationale for the allocation factor chosen.

The costs assigned to each of the Ameren Illinois Utilities are evaluated to ensure the reasonableness of AMS' charges. As described by Company witness Lyons in his direct testimony:

Management personnel of the Ameren Companies review the ongoing status of service requests and the propriety of related costs. In addition, Ameren Services Controller's Department personnel review all service requests and allocation factors on a monthly basis in order to ensure continued applicability of allocation factors utilized and continued accuracy in the assignment of costs to each Ameren subsidiary.

(Respondents' Ex. 2.0, p. 3.)

Ameren Services' Internal Audit Department also audits the service request system and processes every two years. This audit examines the computer systems, billings and source documentation to ensure the services provided are authorized, documented and accurately recorded in Ameren Services' and Ameren subsidiaries' books and records. This Internal Audit Department also examines service request allocation factors to ensure use of such factors complies with SEC guidance and the GSA.

There were a total of 2,712 active service requests during 2004. As shown on Respondents' Ex. 54.6, 1,437 requests received charges during the 2004 calendar year. Further, as shown on the exhibit, each service request has a specific allocation factor. AmerenCIPS was assigned or allocated charges from 480 of the 1,437 service requests which received charges during 2004. Of that amount, 156 were directly assigned to AmerenCIPS. AmerenCILCO was assigned or allocated charges from 435 of the 1,437 service requests which received charges during 2004. Of that amount 96 were directly assigned to AmerenCILCO. Therefore, the number of service requests which allocated charges to the AmerenCILCO and AmerenCIPS is actually a manageable number. (Respondents' Ex. 56.0, pp. 32-33, beginning at line 658.)

The assignment or allocation of AMS' charges are distributed to the Ameren companies via a series of pre-determined allocators. There are 103 Commission-approved allocation factors which could be used to allocate AMS' costs. (Respondents' Ex. 54.7.) Of the 103 allocation factors, 28 had no portion of the costs assigned or allocated to the Ameren Illinois Utilities.

Mr. Adams admitted that the review of AMS' allocations could be daunting, however the task was less difficult when a reasonable approach was taken towards the review. For example, approximately 34 percent of AMS' charges to AmerenCILCO were direct charged. For AmerenCIPS, approximately 23 percent of AMS' charges were direct charged. Further, a mere 181 service requests account for over 80 percent of AMS' total dollars. Of the 181 service requests accounting for over 80 percent of AMS' total dollars, 66 were directly assigned to a specific company. (Respondents' Ex. 56.0, p. 34, beginning at line 688.)

Based upon his knowledge and expertise in the industry, in understanding or knowing what services are needed or required by utilities, Mr. Adams testified that the AMS service requests and allocation factors appear reasonable, and he did not identify any service requests or allocation factors which appeared to be unreasonable. (Respondents' Ex. 54.0, p. 15, beginning at line 331.)

Using the information provided on Respondents' Exhibits 54.6 and 54.7, AMS' costs can be traced to the Ameren Illinois Utilities which ultimately receive the charges associated with the project. Referring to Respondents' Exhibit 54.6, line 28, the service request is titled "Audit of Controllers Operations." As shown in column (C) of the exhibit, the costs associated with this request are allocated using the "017A" allocation factor. Moving to Respondents' Exhibit 54.7, line 99, the exhibit shows that these costs would be allocated to the appropriate entities based upon the number of general ledger transactions. Referring to columns (S) and (T), AmerenCIPS would be allocated 15.25 % of the charges while AmerenCILCO would be allocated 22.15 % of

the costs. Mr. Adams testified that, under this method, AMS and the utility are abiding by the terms and conditions of the GSA. (Respondents' Ex. 54.0, page 16, beginning at line 352)

When the Ameren Illinois Utilities request AMS services as outlined, AMS is obligated to charge according to the requisite allocator. In the end, charges are appropriately assigned to the Company obtaining the service. Respondents' Exhibit 56.2 showed the amount of AMS' charges, by service request, to each of the Ameren companies.

Mr. Adams tested the accuracy of AMS' allocation process, and found that the allocation factors were properly applied for the Ameren Illinois Utilities. (Respondents' Ex. 54.0, p. 16, beginning at line 358.) To test the system, queries were run related to AMS' charges to account 920, broken down by service request and queries of account 920 broken down by feeder reference for the specific companies. From the service request number the allocation factor was traced to the allocation percentage for each Company. The appropriate allocation percentage was multiplied by the amounts produced in the AMS query and checked to make sure that the amount tied to the amount recorded by the Company for the particular project. By this method, Mr. Adams concluded that AMS service charges had been appropriately recorded. (Respondents' Ex. 54.0, p. 16, beginning at line 358.)

Mr. Adams also testified to his belief that both Staff witnesses Burma Jones and Peter Lazare tested or reviewed AMS' costs and allocation process and identified no problems with the methodology and results during these proceedings. No party to these proceedings has questioned the need for a specific service provided by AMS to the Ameren Illinois Utilities. Nor has any party questioned the appropriateness of the specific allocators used by AMS to assign or allocate its costs to the Ameren companies. Finally, no party has identified any allocated cost of specific services for AMS-provided services which were deemed to be excessive, imprudent or unnecessary.

**B. Benchmarking of the Ameren Illinois Utilities' A&G Costs to Other Utilities**

The Commission can also be assured that the level of the costs are reasonable because of the Ameren Illinois Utilities' evidence showing the reasonableness of AMS' costs and describes the steps taken by AMS to evaluate its costs against external providers. To the extent practicable, the Ameren Illinois Utilities have prepared a study comparing their A&G costs with market prices as requested in the Commission's November 21, 2006 order. The study consists of a comparison of the Ameren Illinois Utilities' A&G costs to those of other utilities with comparable characteristics.

This A&G cost comparison identifies (1) a reasonable peer group against which to compare the Ameren Illinois Utilities' A&G costs, and (2) the key variables to be used to develop a peer group of like-sized utilities. Employing information from the 2004 Federal Energy Regulatory Commission's ("FERC") Form 1 annual reports, companies that met the following three criteria were included:

1. Total electricity revenues of between \$200,000,000 and \$1,400,000,000;
2. Total electric customers of between 100,000 and 700,000; and
3. Total MWH sales of between 5,000,000 and 25,000,000.

Based upon these criteria, a peer group of 51 companies, including each of the three Ameren Illinois companies, was selected. Respondents' Exhibit 54.8 sets forth the names, revenues, number of customers and MWH sales for each of the peer group companies. 2004 FERC Form 1 data was used to coincide with the Ameren Illinois Utilities' test year in these proceedings. For the Ameren Illinois Utilities, the test year information as filed in the surrebuttal case was substituted for the information contained in the FERC annual report.

Based upon this data, Mr. Adams compared the Ameren Illinois Utilities' total A&G expenses, excluding Pensions and Benefits costs (Account 926) as a percentage of total

Operations and Maintenance (“O&M”) expenses excluding fuel expenses for each of the peer companies. Pensions and benefits costs were removed because: (1) there is a high level of variability in such costs between companies, (2) the Commission found the Ameren Illinois Utilities’ pensions and benefits expenses to be reasonable in these proceedings, and (3) the Commission’s expressed focus in the Order was on non-pension and benefit A&G costs. Fuel expenses were excluded because of the differences in fuel sources and costs across the country.

Mr. Adams also compared the Ameren Illinois Utilities’ A&G expenses per customer, again excluding the pensions and benefits expenses, to the peer group. This analysis provides insights into the amount each customer is expected to pay related to A&G costs.

Overall, the Ameren Illinois Utilities compared favorably to the peer group. As shown on Respondents’ Exhibit 54.9 (Revised), when comparing the Ameren Illinois Utilities’ test year A&G expenses without pensions and benefits costs to total O&M excluding fuel expenses for the peer group AmerenIP was in the 1st quartile of the peer group while AmerenCIPS and AmerenCILCO were both in the 2nd quartile.

When comparing the Ameren Illinois Utilities’ test year A&G expenses without pensions and benefits expenses per customer to the peer group companies, AmerenIP was in the 1st quartile of the peer group, AmerenCIPS was in the 2nd quartile and AmerenCILCO was in the 3rd quartile. The results of this comparison are shown on Respondents’ Exhibit 54.10 (Revised).

From the benchmarking comparison, Mr. Adams concluded that, overall, the Ameren Illinois Utilities are doing an above-average job of managing the total A&G costs. Most companies strive to be above average in benchmarking analyses. Based upon the results of this benchmarking analysis, the Ameren Illinois Utilities have actually achieved above-average performance in an area that matters most – the amount that each electric customer pays to cover A&G costs. The analysis shows that the Ameren Illinois Utilities are among the industry leaders

in this regard. Thus, far from overpaying for A&G, the Ameren Illinois Utilities are acquiring the services and support they need at cost levels below those of most comparable utilities. This should give the Commission assurance that the charges to the Ameren Illinois Utilities are reasonable.

This benchmarking effort demonstrates the reasonableness of AMS costs charged to the Ameren Illinois Utilities, because the majority of AMS' billings are recorded in the Ameren Illinois Utilities' A&G accounts. Given that the Ameren Illinois Utilities' A&G expenses benchmark compare favorably to those of the peer companies, one can reasonably conclude that the level of A&G costs (including the AMS costs) compare favorably to those of other utilities.

## **V. MARKET STUDIES**

Personnel costs are a significant portion of AMS' overall charges to the Ameren Illinois Utilities, which is not unusual in the industry. (Respondents' Ex. 54.0, p. 21, lines 459-460.) Total personnel costs are a combination of salary levels and total number of employees. To ensure the reasonableness of such costs, market studies are performed related to the salaries paid to AMS employees. For example, to ensure competitive rates of compensation, Ameren's Compensation and Performance Department engages in a market pricing process. This process enables Ameren to leverage information from the external labor market to make internal decisions regarding competitive compensation ranges.

Each year Ameren participates in and purchases numerous salary surveys conducted by reputable third-party vendors (e.g., Towers Perrin, Mercer, Hewitt, AAIM, American Gas Association, Foushee, etc). (Respondents' Ex. 54.0, p. 21, line 472-474) After reviewing, validating and analyzing the data provided by Ameren and other organizations, the survey vendors provide Ameren with detailed reports. These reports provide information about market-

competitive compensation for many positions and often include scope cuts based on industry, revenues, geographical location, and/or discipline.

To market price a position, a member of the Compensation & Performance (“C&P”) team meets with leadership to discuss the nature of the position. The C&P team member then accesses the salary surveys to identify similar positions for which competitive salary data is provided. When available, data from multiple sources is evaluated. The C&P team considers the strength of the survey match and the various scope cuts when evaluating the data and determining a competitive market rate.

The external rate is then reviewed to ensure that it is equitable internally. Once this analysis is complete, an internal “market rate” is set. An employee’s actual pay for the position may be 20 percent below or 20 percent above the internal market rate for the position, thereby defining the competitive market range for the position. An employee’s pay moves through the pay range via the annual merit pay process – which strongly links pay increases with performance.

This process applies to management (non-union) positions. Pay rates for bargaining unit represented positions are negotiated. In cases where the compensation rate for a bargaining unit role is above the market median, the market rates for management positions in the same job family may be adjusted for internal equity.

Respondents’ Exhibit 54.11 provides market data for the majority of positions within AMS for which one or more solid market matches exist. The report includes the title of the AMS position, the 2006 internal market rate for the position, the tentative/proposed 2007 internal market rate for the position (note: 2007 market rates are in the process of being finalized with leadership), the survey title, and the survey match which is aged 2.8 percent (market-reported salary structure movement) to January 1, 2007. The final columns indicate positions for which

internal equity with bargaining unit positions or feeder groups impacts Ameren's internal placement of the position.

The comparisons that are conducted related to the reasonableness of the salaries of AMS employees help to ensure that the wages paid to AMS employees are reasonable given the existing market conditions.

AMS has not performed a study of its staffing levels, because staffing studies are difficult to perform and seldom produce meaningful results. This is due to the fact that the level of staffing at a company is directly proportional to the nature and volume of work required to be performed and the skill sets of the individuals performing the work. Therefore, it is nearly impossible to find a group of comparable companies which provide similar types and volumes of services with similarly skilled people.

While no formal staffing study has been performed, the overall staffing levels at AMS have remained fairly constant despite the acquisition of two additional companies (i.e., CILCO and IP) since 2000. AMS' staffing levels for each of the years 2000 through 2004 are shown on Respondents' Exhibit 54.12.

No party took issue with the wage surveys performed by AMS to assess the market comparability of the wages paid to AMS (and all other Ameren subsidiaries) employees. Nor did any party express concerns regarding the staffing levels of AMS or the Ameren Illinois Utilities. It is significant that no party expressed concerns regarding the staffing levels or the level of wages because the major cost component of AMS' services would be associated with personnel costs. If the wages and staffing levels are deemed to be appropriate, a significant portion of the overall costs would also have to be deemed to be reasonable.

Absent meaningful staffing information, AMS' costs can be evaluated based upon the overall cost of providing a service to assess overall reasonableness. In other words, AMS could

evaluate its costs, on a unitized basis, to the costs of external, non-affiliated providers of similar services. AMS has, in fact, performed such studies. (Respondents' Ex. 54.0, p. 24, lines 523-526) In addition to compensation surveys, periodic studies are performed of AMS' costs against those of non-affiliated providers. Examples of recent studies include:

- Information technology costs and services;
- Disaster recovery/Email archiving costs;
- Help desk services costs;
- Printing and billing costs;
- Lockbox service costs; and
- Accounts payable costs.

Information technology ("IT") costs are an increasing element of almost every company's costs, including AMS. The Ameren Illinois Utilities attempt to gain a competitive advantage by improving productivity and automating processes which have historically been labor intensive. Further, almost every employee now has a computer on his/her desk. In order to maintain the confidentiality and security of company data, the IT group is required to develop, install and maintain security features protecting company programs and data.

IT is also responsible for maintaining a number of the Ameren Illinois Utilities' critical systems. For example, the customer service system would be accessed by customer service personnel that are interacting with customers on a daily basis. The system contains information pertaining to billing information and service history.

Field personnel would utilize automated mapping systems to identify and locate the source of potential problems in the field. The system could also be used to dispatch field personnel to the specific location of an interruption.

Specific to AMS' IT group, the workload has increased significantly in recent years due to merger and acquisition activity. As a result of mergers, it is incumbent upon the IT group to

identify the “best in class” system within the family of companies and to improve, roll-out, and train users on the use of the various systems.

Total cost trends are not the best indicator of AMS’ IT group’s efficiency, because, as mentioned previously, the workload, and thus total cost, has increased in recent years due to merger and acquisition activity. A better indicator of AMS’ IT efficiency is to examine the unit cost trends for the various IT services, which the Ameren Illinois Utilities have done. AMS’ unit costs have been, for the most part, trending downward. In fact, in several cases, costs are below the peer average and approaching or exceeding 1st quartile. Respondents’ Exhibit 54.13 provides a sample of such information. The exhibit shows AMS’ costs associated with Intel servers compared to those of peer companies, both on a total cost basis and on a unit cost basis.

AMS’ IT group has performed a number of studies to evaluate its costs and services. Almost annually, the group retains an external consulting firm to study its costs, workloads, and performance. The findings of these recent IT studies indicate the reasonableness of AMS IT costs:

- Total spending for AMS’ infrastructure environment was 13 % lower than what the workload peer group would spend on average to support the same workload;
- AMS’ cost efficiency relative to the workload peer groups shows improvement;
- Spending on personnel is within range of the workload and utilities peer averages; and
- AMS’ overall staffing level is within range of the Ameren Illinois Utilities peer average.

This study was not a one-time evaluation of the IT group’s costs, but a part of the IT group’s periodic evaluations of its services. Studies indicate that AMS evaluates its performance approximately every other year. (Respondents’ Ex. 54.0, p. 27, lines 584-585.)

AMS also periodically evaluates the level and quality of its services to that provided by external providers. (Respondents' Ex. 54.0, p. 27, lines 587-588.) As a result of such recent studies, AMS has outsourced some IT services. For example, users of AMS' IT services have voiced a strong preference for most of the key IT-related services to continue to be provided internally due to the quality and availability of the service providers. For certain services, however, AMS has found it cost-effective to outsource some services. For example, after evaluating the costs of providing certain disaster recovery/email archiving services internally against the cost of an external vendor providing the service, AMS outsourced certain disaster recovery/email archiving services. As a result of the outsourcing of the disaster recovery/email archiving services, AMS expects to save approximately \$ 1 million over the next five years.

AMS has also outsourced its Help Desk function. (Respondents' Ex. 54.0, pp. 27-28, lines 601-609.) AMS sought competitive bids associated with an external provider potentially offering the help desk services to Ameren family of companies. Based upon the competitive bids, AMS decided to outsource the function to an external provider. The external provider provides service 24 hours a day, seven days a week. The length of the contract is for three years. The contract contains performance metrics which are reviewed monthly. If the metrics are not met on an ongoing basis, the contract calls for remediation. As a result of the outsourcing initiative, AMS was able to reduce headcount by five full-time equivalents.

No party to these proceedings expressed concerns regarding the benchmarking studies performed by the Information Technology Department to assess the reasonableness of its costs.

All of the potential outsourcing studies performed by AMS have not resulted in the decision to outsource a service. (Respondents' Ex. 54.0, p. 28, lines 512-613.) Some of these studies demonstrate that in some instances costs are lower than that which can be obtained from an external provider. For example, AMS sought competitive bids associated with the printing

and mailing of its customer bills. After receiving the bids and analyzing the costs, the conclusion was reached that it remained more cost-effective for AMS to continue to provide the printing and mailing services in-house than it was to outsource the service.

Lockbox service is another example of where AMS' costs to provide a service were more cost-effective than those of external providers. (Respondents' Ex. 54.0, p. 28, lines 615-618.) The lockbox services are associated with the collection, processing and delivery of customer payments to the Ameren Illinois Utilities' banks. AMS solicited competitive bids from external companies to provide lockbox services, and, based upon the results of the solicitation, AMS determined that it was more cost-effective to retain the services internally than it was to outsource the activity.

AMS has examined the possibility of outsourcing its Accounts Payable function to an external, non-affiliated company. (Respondents' Ex. 54.0, p. 29, lines 630-638.) At the time of the review, AMS was in the process of implementing a new system which would interface with the Company's Oracle system. After thoroughly reviewing the pros and cons of outsourcing the activity, decisions were made to: (1) retain the service internal to AMS, (2) continue with the integration of API to Oracle AP, (3) dedicate staff to maximize the electronic enablement of supplier transactions so that Ameren can realize the direct benefits of electronic transactions, and (4) use the information gained from the analysis as a basis to reduce internal costs.

Once the costs of outsourcing a service have been evaluated, AMS maintains contact with external providers. As new providers enter the market or as AMS' cost structure changes, the decision can be made to analyze the feasibility of outsourcing a service. Mr. Adams testified that he is aware of a few companies that have outsourced significant portions of their business or corporate services activities. Such outsourcing efforts have produced mixed results. Typically, the company which is outsourcing the activities seeks to place its employees with the external

vendor. The external vendor would interview the employees and determine which employees to retain. The company would incur severance costs for those employees who are not transferred to the external provider.

Further, many IT-related activities are frequently transferred overseas to obtain lower costs. This represents a loss of jobs to the community and potentially a degradation of service to the company due to language barriers. Mr. Adams testified that, in his experience, such outsourcings of a company's business or corporate services have not produced significant savings to the utility's customers. Based upon discussions with companies that have outsourced significant portions of their business or corporate services, Mr. Adams concludes that such outsourcings have failed to produce the projected levels of savings. In fact, in some instances, the company's costs have actually increased in the short-term due to costs such as severance payments and systems improvements. Achieved savings, if any, would not be realized until the back end of the contractual term of the arrangement. This is not to say that AMS does not seek outsourcing opportunities where outsourcing would be prudent and would produce savings for the utilities. The evidence shows that AMS costs have been shown to be reasonable and AMS is not the sole provider of all services to the Ameren Illinois Utilities.

No party to these proceedings challenged the outsourcing studies performed by AMS to evaluate the costs of its services to those of external providers.

Based upon these findings, it is reasonable to conclude that AMS' costs are reasonable and that the Ameren Illinois Utilities' should be allowed to recover the costs associated with the services that AMS provides. There has been active pursuit of achieving cost savings. The evidence shows that costs are reasonable given the types and levels of services provided, based upon testimony showing the level and types of costs incurred by AMS; the controls which exist at the Ameren Illinois Utilities to manage and control the AMS level of charges; the results of

the comparative benchmarking of the Ameren Illinois Utilities' A&G costs against a peer group of companies; the results of comparative studies performed by AMS such as compensation surveys and IT benchmarking studies; and the results of outsourcing analyses which have been performed by AMS to determine whether its costs were competitive against those of external providers.

## **VI. IMPLEMENTING RATE CHANGES**

In the event the Commission grants a change to the allowed revenue requirement for one or more of the Illinois utilities, as it should, rates should be set to reflect recovery of the new revenue requirement level by using the methodology employed when the Ameren Illinois Utilities filed compliance tariffs subsequent to the November 21, 2006 Order (see pages 149-151). (Respondents' Ex. 53.0, p. 26.) Specifically, the revenue requirement for all three Ameren Companies should be combined to determine the ratio to apply to the Customer and Meter Charges. This will preserve the benefit of uniform Customer and Meter Charges for each separate rate class across the service areas of all three Ameren Illinois Utilities. For example, current test-year base delivery service revenue for the three Ameren Illinois Utilities is \$634.9 million. If the Commission were to grant an additional \$50 million (total for all three Companies), Customer and Meter Charges would all be adjusted upward by 7.9% ( $\$50/\$634.9$ ). Each individual Ameren Illinois Utility would then adjust its Distribution Delivery Charges for each rate class by an equal percentage until the total test-year revenue equaled its authorized revenue requirement.

Further, the \$50.3 disallowance approved by the Commission in its original Order was allocated on an unexplained basis among AmerenCILCO (\$11.267 million), AmerenCIPS (\$15.432 million), and AmerenIP (\$23.601 million). This causes disparate results for the Ameren Illinois Utilities. To the extent the Commission approves adjustments to the Ameren

Illinois Utilities' requested level of A&G expenses, such adjustments should be appropriately based on each of the Ameren Illinois Utilities' share of such costs, rather than based on some other form of allocation. (Respondents' Ex. 53.0, pp. 7-8.)

### **CONCLUSION**

The Order encourages the Ameren Illinois Utilities to provide additional A&G expense evidence on rehearing, and the utilities have done so. Specifically, the Ameren Illinois Utilities have substantiated in excess of \$50.3 million in additional A&G expense costs, from that which was approved by the Commission on November 21, 2006. Much of this evidence on rehearing was not refuted by any party. Further, the Ameren Illinois Utilities have demonstrated the reasonableness of AMS-related A&G expenses, by providing evidence on the reasonableness of 1) the services provided by AMS to the Ameren Illinois Utilities; (2) the appropriateness of the allocation methods, (3) the Ameren Illinois Utilities' A&G expense costs as compared with peer utilities, and (4) AMS market study comparisons. Much of this evidence, as well, was neither directly challenged nor controverted by any party. Thus, the record evidence shows that the Ameren Illinois Utilities have demonstrated their reasonable A&G expenses, in accordance with the Order. The Ameren Illinois Utilities thus respectfully request that the Commission approve the \$50.3 million of A&G expenses disallowed by the Order.

Dated: March 23, 2007

Respectfully submitted,

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

By: Laura M. Earl

One of Their Attorneys

Christopher W. Flynn  
Laura M. Earl  
JONES DAY  
77 West Wacker Drive  
Chicago, IL 60601-1692  
(312) 782-3939

Edward C. Fitzhenry  
Managing Associate General Counsel  
Ameren Services Company  
One Ameren Plaza  
1901 Chouteau Avenue  
St. Louis, MO 63166  
(314) 554-3533

*Attorneys for Respondents*

**CERTIFICATE OF SERVICE**

I hereby certify that a copy of the foregoing was filed on e-Docket and served electronically to all parties of record on this 23rd day of March, 2007.

/s/ Laura M. Earl  
Laura M. Earl, Attorney for the  
Ameren Illinois Utilities