STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

AMEREN ILLINOIS COMPANY d/b/a Ameren Illinois, Petitioner Rate MAP-P Modernization Action Plan - Pricing Annual Update Filing	))))))	Docket No. 12-0293

REPLY BRIEF OF THE STAFF OF THE ILLINOIS COMMERCE COMMISSION

PUBLIC

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TABLE OF CONTENTS

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NOW COME the Staff witnesses of the Illinois Commerce Commission ("Staff"), by and through their undersigned counsel, pursuant to Section 200.800 of the Illinois Commerce Commission's Rules of Practice (83 Ill. Adm. Code 200.800), and respectfully submit their Reply Brief in the instant proceeding.

I. INTRODUCTION/STATEMENT OF THE CASE

A. Procedural History

Section 16-108.5 of the Public Utilities Act ("PUA" or "Act") provides that an electric utility or combination utility (providing electric service to more than one million customers in Illinois and gas service to at least 500,000 customers in Illinois) may elect to become a "participating utility" and voluntarily undertake an infrastructure investment program as described in the Section. A participating utility is allowed to recover its expenditures made under the infrastructure investment program through the ratemaking process, including, but not limited to, the performance-based formula rate and process set forth in Section 16-108.5. (220 ILCS 5/16-108.5(b)) Section 16-108.5(d) of the Act requires a participating utility to file, on or before May 1 of each year, with the Chief

Clerk of the Commission its updated cost inputs to the performance-based formula rate for the applicable rate year and the corresponding new charges, based on final historical data reflected in the utility's most recently filed annual FERC Form 1, plus projected plant additions and correspondingly updated depreciation reserve and expense for the calendar year in which the inputs are filed. (220 ILCS 5/16-108.5(d))

On January 3, 2012, the Ameren Illinois Company d/b/a Ameren Illinois ("AIC") filed with the Illinois Commerce Commission ("Commission") its performance-based formula rate tariff, Rate MAP-P Modernization Action Plan—Pricing Tariff ("Rate MAP-P"). On April 20, 2012, AIC filed its updated cost inputs to the performance based formula rate for the applicable rate year and new corresponding charges.

Initial Briefs ("IB") were filed on September 28, 2012 by the People of the State of Illinois *ex rel.* Lisa Madigan, Attorney General of the State of Illinois (the "AG") and the AARP ("AARP"); the Citizens Utility Board ("CUB"); Staff; and Ameren Illinois Company d/b/a Ameren Illinois (collectively, "AIC"). Some of the issues raised in the parties' initial briefs were addressed in Staff's Initial Brief and, in the interest of avoiding unnecessary duplication, Staff has not repeated every argument or response previously made in Staff's Initial Brief. Thus, the omission of a response to an argument that Staff previously addressed simply means that Staff stands on the position taken in Staff's Initial Brief.

B. Legal Framework and Standards

See Section I (A)

II. OVERALL REVENUE REQUIREMENT

III. RATE BASE

A. Overview

B. Uncontested or Resolved Issues

1. Gross Plant in Service

2. Accumulated Depreciation

3. Cash Working Capital

a. Employee Benefits Expense Lead Days

b. Base Payroll and Withholding Lead Days

4. Materials and Supplies

5. ADIT -- Investment Tax Credits

6. CWIP Not Subject to AFUDC

C. Contested Issues

1. Accrued Vacation Pay

AIC's arguments presented in its IB concerning accrued vacation pay persist in clouding the relevant facts in this case. AIC claims that there is no cash associated with the accrued liability and that it is simply an accounting convention required to recognize the vacation time earned but not taken. (AIC IB, pp. 6-7) In support of its argument, AIC merely offers the same misleading table in its IB that Staff has already addressed as incorrect in rebuttal testimony. (Staff Ex. 6.0, pp. 9-10, lines 179 – 191) The AG/AARP concurs with Staff's opinion of the AIC's exemplary table. (AG/AARP IB, pp. 8-9)

AIC's argument ignores the important fact that the accrued vacation is recorded as a payroll expense and is included in the revenue requirement operating statement on which rates are set. As such, the ratepayers are funding the accrued vacation liability prior to the time the vacation is actually paid in cash. (Staff IB, p. 6) Thus, the shareholders have use of those funds for potentially a year or more. Since AIC did not make a ratemaking adjustment to remove the accrued vacation from payroll expense, AIC admitted that ratepayers have funded the accrual. (*Id*., p. 7)

Since the only additional argument provided by AIC in this case simply serves to support Staff and the Intervenors' positions, the Commission should not stray from its decision in Docket No. 12-0001 on this issue in the instant case.

2. ADIT – FIN 48

AIC states that even though the Commission ruled on this issue contrary to the Company's position in Docket No. 12-0001, it continues to contest the issue in order to preserve its right to rehearing and appeal. (AIC IB, p. 7) AIC claims that the FIN 48 amounts cannot be a cost-free source of capital since interest and penalties must also be accrued on the amount. (AIC IB, p. 8) The record evidence in this case works in opposition to this argument. As discussed in the AG/AARP IB, AIC is not accruing interest on the FIN 48 amounts. "Thus, if the Company is not accruing interest, it must believe that taxes in question will not have to be paid." (AG/AARP IB, p. 11) AIC claims that even though interest is very low or even zero, it cannot be assumed that the FIN 48 amounts are cost free. (AIC IB, p. 9) However, AIC has failed to show what, if any, costs it has incurred associated with its FIN 48 balances.

AIC next claims that ratepayers benefit from the uncertain tax positions taken. (Id.) This benefit, however, does not materialize under AIC's proposal until years after

AIC has taken that position and only after the IRS audit has been completed.[1] In the meantime, only AIC benefits from the use of those funds pending the decision of the IRS audit.

Under the treatment proposed by Staff and the Intervenors, AIC will suffer no risk.

> That is, if some portion of the FIN 48 liability is ultimately paid back to the government, the Company will be made whole when the rate base is reconciled. But as long as the FIN 48 liability is outstanding, it represents a source of non-investor supplied funds to the Company and should be included in the ADIT deducted from the Company's rate base. (AG/AARP IB, p. 12)

The Commission should reaffirm its decision in Docket No. 12-0001 as it is supported by the proposals and arguments presented by Staff, AG/AARP and CUB in this proceeding.

3. ADIT – Projected Additions

The Commission should accept the AG/AARP, CUB, and Staff adjustments to the balance of Accumulated Deferred Income Taxes ("ADIT") to reflect the estimated ADIT associated with the projected 2012 plant additions. The Company illogically argues that ignoring the ADIT associated with the projected 2012 plant additions does not mean that rate base will be "overstated" because by the time rates are in effect for each successive update proceeding, AIC will have *actually incurred* the capital costs for that projected year. (Ameren IB, p. 12) The problem inherent in the Company's position is that the rates resulting from this case will be in effect in 2013 and no data from 2013

[1] For example, the 2005 and 2006 federal tax audits were settled in 2011 and the 2007 audit was expected to be settled in 2012. For these tax periods, under the Company's proposal, only the shareholders would benefit from the deferred taxes until the time the IRS audit decision was issued – approximately 5 years.

is considered within this proceeding pursuant to the formula rate template approved by the Commission in Docket No. 12-0001. In addition, AIC admits that Staff and Interveners' concern is valid from a theoretical perspective that formula rates are to be established based on "actual costs" and reconciled annually with "actual costs." (*Id*.)

The Commission's finding on the issue should be consistent with its prior decisions in Docket Nos. 11-0721 and 12-0001. (Staff IB, pp. 8-9) Accordingly, the Commission should adopt the adjustment to reduce rate base by the ADIT associated with 2012 projected plant additions.

4. ADIT – Step-Up Basis Metro

5. Cash Working Capital

a. Pass Through Taxes Revenue Lag

Staff recommends that the Commission disallow a revenue lag for pass-through taxes. AIC maintains this Cash Working Capital ("CWC") position in spite of acknowledging the resolution of the issue in Docket No. 12-0001, that the revenue lag for pass-through taxes should be zero. (Ameren IB, p. 12)

AIC's initial brief summarizes the same arguments that the Commission rejected in Docket No. 12-0001 (*id*., pp. 15-17). These arguments have been addressed (Staff IB, pp. 11-12), and Staff does not respond again here.

b. Revenue Collection Lag

Staff recommends that the Commission should not set revenue lag at 21 days as proposed by AG/AARP witness Brosch. (AG/AARP Ex. 1.0, p. 21)

Unlike pass-through taxes, AIC relies on the Commission's findings in Docket No. 12-0001 for support of its CWC position in this instance. (Ameren IB, p. 17)

Staff continues to support the collection lag days as proposed by AIC. (Staff Ex. 7.0, p. 6)

c. Income Tax Expense Lead and Lag

Staff recommends that the Commission not set income tax lead and lag days to zero as proposed by AG/AARP witness Michael L. Brosch. (AG/AARP Ex. 1.0, p. 21)

Here again, unlike pass-through taxes, AIC relies on the Commission's findings in Docket No. 12-001 for support of its CWC position. (Ameren IB, p. 19)

Staff continues to support the treatment of deferred income as proposed by AIC which is consistent with Commission practice. (Staff Ex. 7.0, p. 7)

IV. OPERATING EXPENSES

A. Overview

B. Uncontested or Resolved Issues

1. Adjustment for Self-Disallowed Athletic Ticket/Event Expenses

2. Adjustment for Self-Disallowed Regulatory Commission Expense – Docket No. 12-0079

3. Adjustment for EEI Memberships Dues Allocated to Lobbying

4. Account 909—E-store Costs

5. Account 909—Self-Disallowed *Focused Energy.For Life.* Costs

6. Account 909—Employee Book Purchases

7. Account 909—Other Self-Disallowed Expenses

The correct amount of other advertising expenses recorded in Account 909 that AIC has removed from the revenue requirement is $31,609 for 19 items listed in Ameren Ex. 14.3 that include costs for holiday cards, a banking ad for Ameren Energy Management banking, a communication for ERG, street pole banners, photography of the Callaway Nuclear Plant, updated display at Wilmore Lodge at the Lake of the Ozarks, allocated administrative costs to relocate an employee for commercial related work, allocated administrative costs for community related communication and information messaging on renewables, and the editing of a Clean Air Educational video for the Energy Learning Center. (AIC Ex. 14.3) In their IBs, AIC and Staff each set forth different amounts.

AIC stated in its IB that it had removed $48,791 of advertising expenses recorded in Account 909 for activities not related to AIC. (AIC Ex. 14.0, pp. 18-19) Of that amount, $22,165 represented costs referred to as *Focused Energy. For Life* ("FEFL") costs and $26,626 represented costs other than FEFL costs. (AIC IB, p. 22) However, only $17,182 was identified at the rebuttal stage as FEFL costs. (AIC Ex. 14.3 and AIC Ex. 24.0, p. 18, lines 354 - 355) In surrebuttal testimony, AIC did not contest the $4,983 disallowance Staff proposed in its rebuttal testimony; however, the adjustment was not reflected in the Company's revenue requirement schedules since AIC did not update its revenue requirement schedules in its surrebuttal testimony. (AIC Ex. 25, p. 7) In its Initial Brief, AIC excluded from the requested revenue requirement $31, 609 in advertising costs recorded in Account 909 ($48,791from rebuttal testimony less $17,182 from rebuttal testimony = $31,609)

Staff stated that AIC had removed $34,222 of costs for an additional 19 items listed in Ameren Ex. 14.3. (Staff IB, p. 16) However, those nineteen items add to $31,609, rather than $34,222.

8. Adjustment for February 2011 Storm Event

C. Contested Issues

1. Account 909—Advertising Expense

a. *Focused Energy.For Life.* Initiative Costs

The Commission should adopt the positions advanced by Staff and CUB to disallow 100% or $587,000 of FEFL initiative costs. The Company agreed in its surrebuttal testimony that $4,983 of the $587,000 should not be recovered, thus, the contested amount is $582,137.[2] However, the Staff adjustment alters the Company's revenue requirement requested in its rebuttal testimony because the Company did not submit a revised revenue requirement reflecting its surrebuttal position.

The AG/AARP is unsuccessful in its attempt to support the suggestion that AIC recover 50% of FEFL costs "to recognize that these efforts and costs include some messaging that is allowable advertising under the Commission's rules, while also serving the dual purpose of enhancing the Company's image and reputation." (AG/AARP IB, p. 34, emphasis added) The AG/AARP IB points to the rebuttal testimony of its witness, Mr. Brosch (AG/AARP Exhibit 3.3), that included copies of AIC responses to Data Requests ("DR") AG 6.24 through 6.27. It also includes the following example from page 4 of Attachment 5 to the AIC response to DR AG 6.24 that explains why video advertising is used by AIC:

- Help our customers manage their energy use and costs more efficiently.
- Provide our co-workers with a clear understanding of our business and our strategy and how they contribute to our success.
- Generate a more positive perception in the minds of shareholders and encourage them to keep investing in Ameren.

[2] The amount removed for this issue in Appendix A to Staff's IB is $587,000 which includes the $5,000 that AIC self-disallowed in its surrebuttal testimony. Since the Company did not provide new schedules with its surrebuttal testimony, adjustments accepted in Company surrebuttal testimony continue to be included with Staff adjustments in the IB Appendix A.

- Provide regulators and legislators with a more complete understanding of our decisions to assist them as they review pending legislation and rate cases. (*Id*., pp. 34-35)

This appears to be the AG/AARP's only support for its position to allow 50% of the FEFL costs. The only other example it provided is an excerpt from Confidential Attachment 29 to DR AG 6.26 which is a report on "Brand Influence" that reveals that much of the rationale behind investing in Ameren's FEFL program is to increase the value of the Ameren brand. AG/AARP Ex. 3.0 at 39. (*Id*., p. 35) Taken together, these examples do not support disallowance of 50% of FEFL costs. Instead, they support disallowance of 100% of FEFL costs.

In contrast, AG/AARP's IB provided numerous reasons to disallow the entire amount of FEFL costs. These reasons include:

- "…these expenses are not reasonable or necessary for the provision of utility services and should be excluded in setting rates." (*Id*,. p. 32)
- "The emphasis of the ad campaign appears to be intended to promote favorable public opinion of AIC at ratepayers' expense." (*Id*.)
- "…customers need not pay for advertising that reminds them that the utility provides electric delivery services around the clock or that electricity is essential to living." (*Id*., pp. 32-33)
- "If Ameren elects to incur costs in an effort to enhance its public reputation and to remind customers that it is doing its job, these discretionary expenditures should not be included in the revenue requirement." (*Id*., p. 33)
- "Ameren has made no showing that these expenses are prudent, necessary or cost effective in meeting its public utility service obligation." (*Id*.)
- "… a regulated utility has sufficient opportunity through normal communication channels to advise customers of corporate name changes and other factual information…. monthly billings, signage on buildings and vehicles, its web site, numerous call center contacts and other customer contacts provide a utility with an opportunity for regular communication with its customers. There simply is no need for significant additional expenditures to enhance the public image of its brand. As a monopoly energy delivery service provider, it is not as though consumers can switch delivery service providers." (*Id*., pp. 33-34)

The Commission should make the same decision that it made in Docket No. 12-0001, in which the Commission concluded that the FEFL campaign is a marketing campaign that enhances Ameren's corporate image and does not provide benefits to customers. (Staff Ex.8.0R-C, p. 14, lines 281-283; see also generally, CUB Ex.1.0, p. 32, lines 780-795) The Commission's decision in Docket No. 12-0001 is consistent with its treatment of Peoples and North Shore Gas' Safety, Reliability, and Warmth Campaign in Peoples and North Shore Gas' recent rate case where such campaign costs were also fully disallowed. (Docket No. 09-0166/09-0167 Cons., p. 82) A regulated utility has sufficient opportunity through normal channels of communication, such as monthly billings, call center contacts, and its web site, to advise customers of corporate name changes and other factual information and does not need to enhance the public image of its brand. (AG/AARP Ex.3.0, p. 37, lines 787-790)

The FEFL campaign constitutes image building and corporate branding rather than safety, conservation or reliability. Therefore, the Commission should accept Staff's and CUB's recommended 100% disallowance of the FEFL costs.

b. Strategic International Consulting Fees

Staff recommends a disallowance of $73,000[3] that AIC paid to Strategic International Group LLC ("SIG") as advertising costs. AIC claims in its Initial Brief that "[t]here is nothing in the record to support Staff's disallowance and that there is a *bevy of evidence* supporting the reasonableness of the expense. (AIC IB, p. 30) (emphasis added)) However, AIC did not provide any evidence as to the nature of the costs until

[3] Staff's IB showed the amount for SIG as $72,000. Since the actual total was $72,500, rounding to the nearest thousand would be $73,000.

its surrebuttal testimony (Ameren Ex. 24.0, pp. 13-14) and the cross-examination of its witness (Tr., September 12, 2012, pp. 146 – 147) even though Staff proposed the disallowance in its direct testimony. This strategy on the part of AIC prevented any party from having an opportunity to respond to the support provided by the Company. The evidence provided by AIC in its surrebuttal testimony and the cross-examination of its witness does not support the reasonableness of the expenses at issue and does not change Staff's recommendation for disallowance.

The "bevy of evidence" submitted by the Company provides generic and conflicting descriptions of the work that was to be performed by SIG. The AIC purchase order (Staff Cross Exhibit 3) authorizing the payment of funds to SIG indicates the work was to "Facilitate communications to diverse audiences for various customer related programs: EE and energy assistance in accordance with Scope of Work 1." The unsigned contract provides only what appears to be generic contract language, the supplier name identified as "Strategic International Group Attn: Emil Jones", the supplier address, and the Scope of Work Number 1 which is stated as follows:

> From March 1, 2011 to February 29, 2012, Strategic International Group will provide consulting and management services specific to issues facing the Client in the areas of **government relations and issues management**. It is expressly understood that the Services under this contract shall not include any lobbying activities as defined by local, state and federal laws.

(Staff IB, p. 19) (emphasis added)) Nothing in the unsigned contract with SIG indicates any required work on energy efficiency, conservation or customer programs which was alleged to have been provided by SIG in the submitted AIC purchase order. (Staff IB, p. 20) The purchase order does not agree with the terms of the contract and, thus, calls into question the services SIG was alleged to have performed in exchange for the payments received from AIC.

AIC offers for the first time in its IB the absurd and off-point claim that Staff did not contend that energy assistance charges are not recoverable. Since AIC didn't allege that energy efficiency and conservation related matters were the purpose of SIG's consulting services prior to its surrebuttal testimony, Staff had no reason to make such a contention in its direct and rebuttal testimonies. (*Id*., p. 29, citing AIC Ex. 24.0, p. 14) In addition, if SIG provided energy efficiency related services, the costs would be eligible for recovery through Ameren's energy efficiency rider.

Equally without merit is AIC's assertion that the contract with SIG "meets the letter, if not the spirit of the law." (AIC IB, p. 29) AIC has failed to carry its burden of proof for the advertising expense related to SIG and those expenses should be disallowed. (Staff IB, p. 20)

The Commission should adopt Staff's recommended disallowance of $73,000 of advertising expense AIC paid to SIG.

c. Purchase Card Expense

The Commission should accept the Staff disallowance of $27,000 of unsupported Purchase Card ("P-Card") expenses. AIC sought recovery of P-Card Expenses totaling $102,000 and only provided brief descriptions to explain $75,000 of the total costs[4]. In rebuttal testimony, Staff proposed a disallowance of the remaining $27,000 that AIC did not support. (Staff Ex. 8.0R-C, p.12-13, lines 240-254)

[4] Part of the $75,000 explained by the Company is the $4,387 for books addressed in the uncontested section of this IB.

The extensive cross-examination conducted by the ALJs and the responses provided by AIC witness Pagel cast doubt on the recoverability of any portion of the P-card costs based on the requirements of the Act. (Tr. September 12, 2012, pp. 136 – 166) Ameren has failed to associate any of the P-Card expenditures in any way to advertisements or advertising campaigns. Thus, it is impossible to determine whether the expenses are recoverable under section 9-225 of the Act as an advertising expenditure. AIC asserts that it should not need to provide any nexus between the expenses and the advertisements or advertising campaigns. (AIC IB, p. 31) This is in violation of 220 ILCS 5/9-227, which requires the Company to make available to the Commission all materials supporting "[a]ll expenses incurred by the utility included in the operating expense for ads or scripts produced by a trade association including all monies paid to the association for advertising purposes, either in the form of dues, assessments or subscriptions." Staff reiterates the argument presented in its IB, that AIC appears to believe that simply because costs have been paid (and approved by a supervisor) they are reasonable for recovery as advertising expense. When the charges in question are incurred primarily for meals, purchases at retail stores (Best Buy, Dollar-General, Office Max, Lands End Business, Bees and Blooms) lodging and gasoline, and AIC refuses to provide any indication of the relationship between these costs and advertisements or advertising campaigns, the automatic recovery AIC suggests for such costs must be questioned. (Staff IB, p. 20)

Furthermore, AIC admits that it does not track or code P-Card charges booked to Account 909 to specific advertisements, yet it demands that with no support, it should be allowed to recover those amounts from ratepayers since it would require too much effort to track those items. (AIC IB, pp. 30-31) This argument advanced by AIC suggests that in order for such costs to be recoverable from ratepayers, the internal controls for P-Card charges must be reevaluated to conform to rules established for costs designated as advertising.

AIC states in its IB that Staff's request to identify each P-Card purchase of $200 or less with a specific advertisement is not the evidentiary standard for disallowing advertising expenses. AIC continues that the evidence is neither readily available nor necessary for AIC to carry its burden of proof that these expenses are recoverable business expenses. (AIC IB, p. 30) What AIC fails to appreciate, however, is that in seeking to recover these costs as advertising costs, it has a higher standard to meet than is the case for other business expenses. Section 9-225 of the Act states that "the Commission shall not consider, for the purpose of determining any rate, charge of classification of costs, any direct or indirect expenditures for promotional, political, institutional or goodwill advertising, unless the Commission finds the advertising to be in the best interest of the Consumer" or is included by the Commission as an allowable category of advertising as set forth in Section 9-225(3). (220 ILCS 5/9-225) The Commission cannot determine whether these costs are in the best interests of the consumer because AIC has not provided any indication as to the nature of those costs as required by Section 9-225.

Another unfounded argument advanced by AIC in its IB is the concept of an "underlying current in Staff's review that the utility's burden is to document and support every dollar charged to Account 909". (*Id*., p. 32) This is false. In fact, Staff had only one goal—to review the advertising costs AIC requested for recovery in this proceeding, in compliance with Sections 9-225 and 9-227 of the Act. While AIC whines and describes Staff's review as "unprecedented relative to prior reviews done in prior rate proceedings …" the review was similar to the review that Staff typically undertakes and, in this case, Staff provided AIC every opportunity to support its costs. The Company continues to complain that "…more information has been provided in less time and with greater detail." (*Id*.) Given the inadequate support provided by AIC as explained here and in Staff's rebuttal testimony, AIC is apparently advancing a new, lower evidentiary standard that requires the utility to provide only that which is readily available. (ICC Staff Ex. 8.0R-C, pp. 12-13, lines 237-254)

The Commission should carefully consider whether the Company has met its burden of proof for the costs paid by P-Card and adopt Staff's position to disallow the unsupported costs.

2. Account 930.1—Corporate Sponsorships

The Commission should adopt the adjustment of AG/AARP and CUB to disallow the remaining jurisdictional corporate sponsorship costs because these are discretionary expenses not required for the provision of utility services. Such sponsorship amounts to "goodwill advertising" expenses, which are to be specifically excluded from rates under Section 9-225 of the Act. (AG/AARP IB, p. 36) After consideration of the arguments presented by the AG/AARP and CUB in their IBs (AG/AARP IB, pp. 35-37 and CUB IB, pp. 17-20), Staff recommends that the Commission disallow all corporate sponsorship costs and not just the $54,000 in corporate sponsorship costs reflected in Staff Ex. 8.0R-C, Schedule 8.04.

AIC in its IB disputes the claims of Staff, AG/AARP, and CUB that AIC's corporate sponsorship costs in general are image building, institutional advertising expenses that should be disallowed, regardless of whether AIC received tickets in return for its sponsorship. (AIC IB, p. 33) The record evidence, however, does not provide support that such corporate sponsorship costs can and should be reasonably recovered from ratepayers. The following examples of such corporate sponsorship costs speak for themselves:

- Attendance of Ameren representatives at the Wine and Polo on the Prairie for the Easter Seals of LaSalle and Bureau County in which the attendees drink wine and watch polo (Tr., September 12, 2012, pp. 167-168);

- Attendance of Ameren representatives at the Lewis & Clark Community College Golf Classic where the representatives played golf (Tr., September 12, 2012, p. 168);

- Attendance and dinner for fifty people at the induction of Scott Cisel into the African American Hall of Fame Museum to recognize Scott Cisel for his work with diversity in the Peoria/Greater Peoria area (Tr., September 12, 2012, pp. 169-170); and

- Costs for an anniversary book to document the history of the Ameren legacy companies (Central Illinois Light Company, Illinois Power Company, Central Illinois Public Service Company, and Union Electric) that was distributed to employees of Ameren and available to customers who were interested in the history of the company (Tr., September 12, 2012, p. 171).

AIC avers the Commission's Order in Docket No. 12-0001 is incorrect as a matter of fact and policy because it believes its corporate sponsorships "bring AIC's name before the public in a philanthropic light." It notes further that the Commission has previously found that "public recognition" for a utility's support of civic events does not mean the associated costs are *per se* unrecoverable and subject to a blanket disallowance (AIC IB, pp. 33-34). However, the evidence in this case (some of which is cited *supra*) proves that the utility received benefits from the corporate sponsorships and, therefore, the costs for such corporate sponsorships should not be recovered from ratepayers. (Staff IB, pp. 21-23, AG/AARP IB, pp. 35-37, and CUB IB, pp. 17-20)

Ameren argues that the parties "should review the material provided by the utility for these events on a case-by-case basis, and not throw the baby out with the bathwater." (AIC IB, p. 35) The documentation AIC has submitted in support of its corporate sponsorships, however, has been individually reviewed and has been shown by the parties to be inappropriate to recover from ratepayers.

3. Formula Rate Case Expense—Docket No. 12-0001

Amortization Period

AIC states that recovery of rate case expense for the initial performance-based formula rate proceeding should be amortized over a three-year period. (AIC IB, p. 38) Staff agrees with that statement and provides for a three-year amortization for costs incurred in 2011, since the costs being considered in this docket are those incurred during 2011. Under Staff's proposal the costs that are incurred for the initial performance-based formula rate proceeding will always be amortized over a three-year period beginning in the year those costs are incurred. (Staff IB, p. 23) Since AIC filed an Application for Rehearing in Docket No. 12-0001 on October 3, costs for the initial performance rate proceeding will extend into 2013 and those costs would also be considered for recovery, based on the year incurred. AIC's proposal is silent as to how it would seek to recover costs incurred beyond 2012 associated with Docket No. 12-

0001, only addressing costs incurred in 2011 and 2012 to be amortized beginning in 2012. (AIC IB, p. 38)

AIC claims that since it filed its initial performance-based formula rate proceeding in 2012 rather than in 2011 (as did ComEd) the rate case expense amortization period should not begin until 2012 even though the rate case expenses were incurred in 2011. Nothing in the EIMA provides for the amortization of all the costs of the initial proceeding to be amortized beginning in the year it was filed as opposed to the year they were incurred. In fact, Section 16-108.5(c)(4)(E) anticipates that "subsequent proceedings related to the formula" would also be recovered over a three-year amortization period:

> (E) recovery of the expenses related to the Commission proceeding under this subsection (c) to approve this performance-based formula rate and initial rates **or to subsequent proceedings related to the formula, provided that the recovery shall be amortized over a 3-year period**…(emphasis added)

AIC's claim that it would forego its ability to recover 1/3 of the approved 2011 rate case expense under Staff's proposal should likewise be rejected. Staff has already identified the fallacy of that claim in the explanation of the reconciliation process in its IB and will not repeat it here. (Staff IB, pp. 24-25)

Staff's proposal for the three-year amortization period for rate case costs incurred in 2011 should be approved by the Commission.

<u>Disallowed rate case expenses</u>

In its IB, AIC only discussed the legal fees that Staff was removing from the total 2011 rate case expenses to be amortized. Section 9-229 of the Act requires the

Commission to assess the justness and reasonableness of any amount expended by a public utility to compensate attorneys or technical experts to prepare and litigate a general rate case filing (220 ILCS 5/9-229) and in its in Final Order in ICC Docket No. 10-0467 the Commission noted:

> All utilities would be advised to provide, at the very least, an explanation of what services were performed, the amount of time involved in performing those services, and the need for whatever service was performed in order to justify rate case expense.
>
> (Final Order, Docket No. 10-0467, May 24, 2011)

AIC argues that Staff, and ultimately the Commission, should accept redacted invoices to support the recovery of outside legal fees because those invoices contained information that was designated by AIC as confidential and proprietary. (AIC IB, pp. 36-37) AIC does not, however, explain how this confidential and proprietary designation gives Staff and the Commission sufficient information to determine the justness and reasonableness of the rate case expense. Staff is not asking the Company to disclose privileged information; Staff is merely asking the Company to provide enough support to justify the inclusion of these costs in rate case expense.

With regard to those invoices that were not heavily redacted, AIC claims that most of the legal descriptions could be easily reviewed. (*Id*., p. 37) This argument does not reach the heart of the issue. AIC fails to explain why the examples of costs that Staff pointed out as *unrelated* to the initial proceeding should be approved for recovery. (Staff IB, p. 25) AIC also fails to explain how it would determine what portion of a complex individual entry on the legal bills is properly recoverable. Some bills contain descriptions of multiple activities within one charge, some of which may be recoverable, and some of which may be found not to be recoverable.

Additionally, AIC failed to address Staff's concern regarding the cost for meals for Concentric Energy Advisors that were included in rate case expense for Docket No. 12-0001. Based on the Company's agreement that these costs should not be included in rate case expense (Ameren Ex. 19.0, p. 3, lines 45 – 46), the Commission should make note that this type of cost from Concentric Energy Advisors will not be recoverable as rate case expense in subsequent formula rate cases. (Staff IB, p. 25)

4. Regulatory Commission Expense—Docket No. 11-0279

AIC claims that the costs it incurred associated with the preparation and litigation of Docket No. 11-0279, the electric rate case that was withdrawn in early 2012, should be recovered in full from rate payers in this proceeding because the costs were incurred in 2011. (AIC IB, p. 40) A review of the costs beginning on Page 2 of 501 of Ameren Late-Filed Exhibit 1 indicates that the costs were actually incurred as early as July 2010 and extended in some cases through March 2012.[5] While the costs were being incurred, AIC deferred them as regulatory assets. At the end of 2011, when AIC decided to withdraw the rate case filed as Docket No. 11-0279, the costs were reclassified to Account 928 and, thus, included in 2011 operating expense even though the costs were actually incurred over a period of three years.

[5] It is unclear how the costs for periods after December 2011 were included in the rate case expenses or reported on FERC Form 1 for the year ended December 31, 2011 as reported on Ameren Late-filed Exhibit 1.

AIC claims that the cost components of the Docket No. 11-0279 rate case expense were already reviewed and approved by the Commission. (AIC IB, p. 42) AIC also claims that:

> The Commission found the **exact same information** which supports recovery of the electric portion of AIC's rate case expense in those dockets to be "extensive" "ample and credible information" sufficient to support recovery of the gas portion. (AIC IB, p. 46) (emphasis added)

While Staff does not disagree that the Commission approved rate case costs for recovery in the AIC gas rate case Docket No. 11-0282[6], which are the same type of costs being requested for recovery now, certain additional evidence has been presented for the Commission's consideration in the instant case.

The "exact same information" provided in Docket No. 11-0282 is not in evidence in this case. AIC agreed that many of the invoices to support actual costs were provided for Staff review for the first time in this proceeding (Staff Cross Ex. 1). In addition, Staff offered a thorough discussion of the shortcomings found in the evidence provided both in testimony, (Staff Ex. 6.0, pp. 15-19, lines 292 – 384), and summarized in Staff's IB. (Staff IB, pp. 27-28) Even the Company agreed that a portion of the rate case costs that were approved for recovery in Docket No. 12-0282 (consultant charges for meals) should not be recovered in this proceeding. (AIC IB, p. 20)

AIC continues to take issue with Staff's proposed disallowance of costs to CCA for "witness development skills". During cross-examination, however, AIC witness Nelson admitted that two of the four witnesses he had listed as inexperienced, (AIC Ex.

[6] No decision was made for cost recovery of rate case expense for Docket No. 11-0279 since the Company chose to withdraw that case prior to a final order being issued.

18.0, p. 17, lines 352 – 355), have worked for the Ameren Companies for over 20 years and have testified a number of times before the Commission. (Tr., September 12, 2012, pp. 44 – 50) For the other two witnesses he listed as inexperienced, Mr. Nelson admitted that he did not know if the witnesses had testified before any regulatory bodies prior to their employment at Ameren and had to some extent based his testimony on discussions with counsel as to the experience level of these witnesses. (*Id*., pp. 42 - 44 and pp. 51 – 52) Mr. Nelson next explained that he, himself, (Id., pp 52-53) along with AIC witnesses Stafford, Mill, and Jones also participated in the training by CCA. AIC witnesses Nelson, Stafford, Mill, and Jones are all experienced witnesses before this Commission. (*Id*., pp. 54 – 56) The argument that additional training is necessary for these experienced witnesses is without merit.

AIC mischaracterized responses by Staff witness Ebrey regarding her preparation for cross-examination in this case, inferring that her preparation for the hearing in this case was comparable to the training provided by CCA. (AIC IB, pp. 45-46) During redirect, Ms. Ebrey clarified the various steps she takes to prepare for taking the stand for a typical case.

> Q. Okay. And then just very briefly, you were asked questions about what you do to prepare for testifying, and I don't know if you were specifically asked that question, but what is it that you do in order to be put on the stand for a typical case?
>
> A. I prepare my book with my testimony, my responses to data requests that came from the company or from other parties. I read my testimony to make sure I'm familiar with it as well as my responses. I read the company testimony that I've replied to in the testimony that I have filed. You know, I consider which issues may be more contentious than others and try to anticipate questions the company may ask me and think of what my responses will be.

> Q. Okay. And then do you have any outside assistance in terms of preparing for your testimony?
>
> A. If you mean outside the agency, outside training?
>
> Q. Well, I guess both outside the agency and within the agency.
>
> A. There's no formal training that I've had. No outside parties have come in and provided any training for witnesses. If I have some issues that I'm unsure about, I may talk to my supervisors, you know, here's something that I'm concerned about. How do you think I should address this, or does this sound reasonable. You know, I speak with other, more experienced people at the Commission. (Tr. September 13, 2012, pp.444-445)

The training for 9-12 participants and 3 consultants provided thru CCA as outlined on the support provided went well beyond Ms. Ebrey's preparation for the hearing:

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> (Ameren Late-filed Exhibit 1 CONFIDENTIAL and PROPRIETARY, pp. 404 and 405 of 501)

AIC's attempt to draw a parallel between AIC witness training and Staff witness preparation falls short.

Staff again urges the Commission to disallow the rate case expense costs associated with Docket No. 11-0279 for all the reasons previously discussed in its testimony and IB. However, if the Commission determines that rate case expense costs for Docket No. 11-0279 are recoverable in the instant case, that amount should be limited to $2,293,000 as set forth on Staff Ex. 6.0, Attachment A for the reasons discussed in Staff's IB. (Staff IB, p. 25)

5. Deferred State Income Tax Expense

All parties agree that the only remaining issue related to the Deferred State Income Tax Expense is how to reflect it in the revenue requirement in this case. AIC selectively chooses to highlight the treatment of Electric Distribution Tax in Docket No. 11-0721 where the accrual of tax credits recorded by ComEd in 2010 was deferred and amortized over a five-year period, (ComEd Docket No. 11-0721, Order, May 29, 2012, p. 108), claiming the Commission decision here should be consistent with that Order. AIC did not, however, offer **any** explanation why the Commission should provide the same regulatory treatment for Deferred State Income Tax expense in the current AIC case that was provided for ComEd's anticipated refunds for the Illinois Distribution Tax, which is a totally distinct and different tax issue than the one at issue in this proceeding.

As indicated in the AG/AARP IB, "Unusual, extraordinary events or costs that are non-recurring in nature are often considered for deferral and amortization ratemaking, so as to spread out and 'normalize' the amounts included in revenue requirements to be paid by customers." (AG/AARP IB, p. 45) The Deferred State Income Tax Expense treatment at issue here does not pass that test. As CUB pointed out:

> …the impacts on deferred state income tax expense related to the known changes in the state income tax rate are annually recurring, and are not an isolated impact confined to calendar year 2011 but rather create additional annual reductions in 2012 through, at least, 2024. (CUB IB, p. 23)

For the above reasons and those explained in Staff's IB (Staff IB, pp. 28-30) and consistency with the treatment proposed by ComEd, and agreed to by the parties, for this identical issue concerning the Company benefit resulting from the Deferred State Income Tax in ComEd Docket No. 12-0321, the adjustments proposed by Staff and the Intervenors should be approved.

6. Section 9-227 Donations/Charitable Contributions

AIC's entire argument against Staff's proposal to disallow ten donations from the revenue requirements is based upon the following:

> The basis for Staff's adjustment in this proceeding is the same basis rejected by the Commission in Docket No. 12-0001: the use of the recipient's federal tax status as a filter to exclude from rates the donations that utilities make to economic development organizations.
>
> (AIC IB, pp. 50-51)

AIC's argument fails, however, because the federal tax status filter was not the only criteria used by Staff to conduct its Section 9-227 analysis.

Staff openly acknowledged in its Initial Brief, (Staff IB, p. 31), that the Commission rejected the notion of an Internal Revenue Code Section 501(c)(3) status as a "filter." In its Docket No. 12-0001 Order, the Commission stated that for a donation to meet the Section 9-227 "public welfare" requirement, it must benefit the rate paying public in AIC's service territory. (Final Order, Docket No. 12-0001, p. 79) Staff's further analysis of the charitable contributions recoverability from ratepayers addressed that criterion. (Staff IB, pp. 31 - 32) AIC bears the burden of providing sufficient evidence that such donations meet the requirements of Section 9-227; but, it has failed to do so.

Staff demonstrated in its Initial Brief that membership fees to tourism commissions and economic development organizations are not donations because AIC receives a corporate, not a public welfare, benefit from making these donations. (*Id*.) Staff pointed out that the corporate benefits Ameren received range from receiving member discounts to being involved in joint efforts to shape public policy and key issues affecting their businesses and their community. (*Id*.) For example, the home page for the Greater Springfield Chamber of Commerce at http://www.gscc.org/join/benefits.asp states:

> Membership in the Greater Springfield Chamber of Commerce offers significant opportunities to grow your business, hear from the region's prominent business and government leaders, and expand your contacts.

It is evident that corporations receive a benefit from being members in these organizations. The benefits range from receiving member discounts to being involved in joint efforts to shape public policy and key issues affecting their businesses and their community. What is not described on the mission statement or home page is its charitable mission, or how the public welfare benefits from the organization.[7]

These benefits aid the company; they do not aid the rate-paying public in AIC's service territory. (*Id.)* AIC alleges that these economic development organizations enhance local communities by attracting new industry and jobs, and assist companies in relocating and expanding. (AIC IB, p. 53) It is highly improbable, however, that the vast majority of AIC ratepayers could identify any benefit they have enjoyed from these donations. Moreover, based on the corporate tax structure policies of the State of

[7] (Staff Ex.8.0R, pp.8-9)

Illinois[8] and various other units of government[9] it is likely that the economic development opportunities fostered by these organizations in their respective communities is done at the expense of the loss of economic development in other Illinois communities, some of which may also be in Ameren's territory. For example, organizations such as the municipal chambers of commerce that AIC donated to often attract jobs away from another State Municipality, which may also be in AIC's service area. Again, it is very difficult to see how this would benefit the public welfare of the state as a whole or even the more limited public welfare of those paying AIC rates. At best, it would be a wash with the jobs leaving one city for another city within the AIC service territory. In short, these donations do not benefit the public welfare.

The Commission has previously concluded that payments to economic development organizations disguised as charitable contributions should not be recovered from ratepayers. In these orders, the Commission explicitly found that it "is not willing to blur the distinguishable categories of industry dues and charitable contributions." In the orders cited below, the Commission concluded that the specific contributions to economic and community development organizations at issue were more properly categorized as an industry dues that should be shouldered by shareholders:

In the Final Order in Docket No. 05-0597, the Commission disallowed a $50,000.00 donation to the Illinois Manufacturers' Associations (IMA). The Commission

[8] The Tax Increment Allocation Redevelopment Act (65 ILCS 5/11-74.4.1 et seq.), The Economic Development Project Area Tax Increment Allocation Act of 1995, (65 ILCS 110/1 et seq.), Business District Development and Redevelopment Act (65 ILCS 5/11-74.3 et seq.).
[9] County Economic Development Project Area Tax Allocation Act (55 ILCS 85/).

explained that because the payment constituted a payment for lobbying or a political activity:

> ComEd claims that this contribution was for the IMA's "Research on Education in Illinois" and that Staff's adjustment for this should be rejected. Staff argues that the invoice is clearly labeled a "Legislative Strategies" contribution. *Section 9-224 of the Act (220 ILCS 5/9-224) prohibits including in any rate or charge any costs or payments for lobbying or political activity.* Therefore, the Commission will reduce the revenue requirement for ComEd by $50,000.00.
>
> (Docket No. 05-0597 ComEd Order, p. 103 (emphasis added))

Likewise, in the Final Order in Docket No. 04-0442, the Commission upheld a Staff disallowance for an amount paid to the Danville Area Economic Council. The Commission found that the payment was within the category of dues and not charitable contributions. The Commission explained that:

> The first area of the adjustment concerns the amount paid to the Danville Area Economic Council. This type of adjustment also was at issue in Docket 03-0403. The Order entered in that case states:
>
> > *The Commission is not willing to blur the distinguishable categories of industry dues and charitable contributions. The Order entered in 90-0169 squarely places the costs for industry association dues on the shareholders. See* Order, 90-0169, at 65.
>
> *The Commission finds that the payments to the Danville Area Economic Council are within the category of dues and not charitable contributions. The eventual public purpose, as alleged by Aqua, is insufficient to qualify the dues paid for recovery pursuant to Section 9-227.* The Commission therefore holds that the adjustment proposed by Staff is proper for the payments to the Danville Area Economic Council.
>
> (Final Order, Docket No. 04-0442, p. 31 (emphasis added))

Again, in the Final Order in Docket No. 03-0403, which concerned Consumers Illinois Water, the Commission adopted Staff's adjustment to charitable contributions because it lacked sufficient evidence to determine that the contributions to the community and economic development organizations were properly within the scope of Section 9-227. The Commission explained that:

> *Neither party contends that the donations at issue are for "charitable scientific, religious or educational purposes." Instead, they are for community or economic development associations.*
>
> *   *   *
>
> *The Commission declines to presume that, at any given local unemployment rate, contributions to economic and community development organizations are necessarily for the public welfare.* It is possible that such a contribution is made for a purpose that can not be recovered under Section 9-227. The Commission specifically notes, however, that it also does not establish any rule or presumption that contributions to economic and community development organizations may not be recovered under Section 9-227. Instead, a determination must be made on the evidence presented for each case. The utility has the burden to provide the evidence required to establish recoverability under this Section.
>
> *   *   *
>
> *With only the basic information contained in Schedule C-7 and Company testimony regarding other donations not at issue here, the Commission lacks sufficient evidence to determine that the contributions to the community and economic development organizations are properly within the scope of Section 9-227*. Accordingly, the Commission concludes that the amounts in question should be excluded from the cost of service in this case. (Cf. Order, 02-0690, at 21 (disallowing recovery of donations "which may or may not be allowable under the Act, but [due to the] lack of evidence, cannot be determined as such"). Accordingly, Staff's proposed reduction to charitable contributions is accepted.
>
> (Final Order, Docket No. 03-0403, pp. 18-19 (emphasis added)).

And, another example in which the Commission concluded that dues to chambers of commerce and community organizations may not be characterized as charitable contributions is found in the Final Order in Docket No. 01-0432, which concerns Illinois Power Company:

> A significant component of Staff's argument on this issue is that IP will receive membership benefits in return for the dues payments in question. Notably, IP did not refute this assertion. The Commission concurs with Staff's recommended disallowance of $56,000 of chambers of commerce and community organizations dues. Since IP benefits from the payment of the dues, they may not be

> characterized as charitable contributions. Whether or not the IRS considers the organizations to which the dues payments were made not-for-profit is not at issue.
>
> (Final Order, Docket 01-0432, March 28, 2002, p. 54)

Clearly, the donations at issue in this proceeding, which Staff seeks to disallow, suffer from the same infirmities as those charitable contributions addressed by the Commission above and further do not meet the Commission's idea of a Section 9-227 "public welfare" definition as articulated in its 12-0001 Order. In sum, at best, any alleged benefit to the public welfare is remote and tenuous. On the other hand, the benefits the Company enjoys from these donations are direct and clear.

Staff recommends that the Commission accept Staff's proposed adjustment to remove from the Company's revenue requirement the donations to the ten economic development organizations listed on Staff IB, Appendix A, Schedule 11, page 2 because they are not charitable contributions to be reviewed under the criteria established in Section 9-227 of the Act.

V. REVENUES

A. Uncontested or Resolved Issues

B. Contested Issues

1. Late Payment Revenues

The Company argues that since AG witness Brosch did not reduce the revenue requirement for power supply costs, the adjustment to include 100% of late payment revenues in the revenue requirement is asymmetrical and unfair. (AIC IB, pp. 54-55) The Commission considered and rejected this same argument in its Analysis and Conclusions in ComEd Docket No. 10-0467:

> Staff's and ComEd's argument on this issue appears to be that, because ComEd is only in the business of delivery services (the cost of the actual electricity being procured from other entities and billed at approximately actual cost), any profits (late payment charges) that ComEd makes from the electricity delivered cannot reduce ComEd's revenue requirement, even though all parties seem to agree that ComEd actually received these late payments charges, and, that it receives a profit upon both delivery services and the actual electricity it procured, in the form of these late payment charges. No party has stated any legal basis for ignoring this reality. In fact, it appears that the argument proffered for excluding the $13.986 million ignores common sense.
>
> ComEd has classified the $13.986 million as non-jurisdictional. However, as CUB points out, the only "other jurisdiction" that ComEd is subject to is the FERC. Yet clearly, except for $2 million, which was accounted for by Mr. Effron, these are not FERC-related charges. Additionally, ComEd is in the business of delivering electricity. In that capacity, to many customers, it provides the electricity to deliver. Therefore, whether the late charges are upon delivery charges or upon the electricity delivered, they are imposed to the delivery service that ComEd provides to the individual customer involved.
>
> To illustrate the fallacy of ComEd's argument, the Commission points out that a consumer's total bill has many charges, including such items as those for state and local taxes. The interest charge is imposed on all of these charges. Yet, it cannot be said that state and local taxes are non-jurisdictional. The Commission concludes that ComEd has failed to establish, on an evidentiary basis, that a portion of these charges is not jurisdictional.
>
> (Docket No. 10-0467, Order, May 24, 2011, p. 305)

AIC attempts to show how the record evidence in this case differs from the ComEd case quoting the Order in Docket No. 10-0467 that ComEd was not able to identify how the late payment revenues were **credited to customers** or otherwise accounted for. (AIC IB, p. 55) Staff believes this quote is instructive for approving the Staff, AG/AARP and CUB adjustment. AIC, like ComEd in the cited docket, did not provide any evidence in the record to identify how AIC's late payment revenues are credited to customers. Instead, AIC continues its proposal to delay reflecting over 55% of the late payment revenue until some unnamed time in the future. (AIC IB, p. 56) That suggestion was already rejected by the Commission in its Order in Docket No. 12-0001.

> In order to prevent an under recovery in certain areas, AIC suggests that other adjustments may be necessary if AG/AARP's proposal is adopted. AIC recommends denying AG/AARP's recommendation and reconsidering it and other appropriate adjustments, including adjustments to Rider PER, in the context of a future rate redesign proceeding to be initiated under Section 16-108.5(e) or at the time of the next Rider PER update filing. In the absence of compelling evidence that such other adjustments are necessary; however, the Commission is not inclined to wait to address this shortcoming in the adjustments to AIC's revenue requirement. Retaining for shareholders 58% of late payment revenues supplied by ratepayers is a disservice to ratepayers. The Commission accordingly adopts the AG/AARP adjustment on this issue. Furthermore, the Commission notes that this outcome is consistent with how similar revenue is treated for ComEd's revenue requirement calculation. (Docket No. 12-0001, Order, September 19, 2012, p. 106)

The Commission should reach the same decision to reflect 100% of the late payment revenues in its decision here, consistent with its decisions in ComEd Docket No. 10-0467 and AIC Docket No. 12-0001.

VI. RATE OF RETURN

A. Overview

B. Uncontested or Resolved Issues – Capital Structure/Rate of Return

1. Rate of Return on Common Equity

2. CWIP Accruing AFUDC Adjustment

3. Cost of Short-Term Debt, Including Cost of Credit Facilities

AIC errs in its IB by applying Ameren Corp.'s 2.30% cost of short-term debt to AIC's zero short-term debt balance, which AIC asserts is set in accordance with the order in Docket No. 12-0001. (AIC IB, Appendix A, p. 13, lines 8 and 20; AIC IB, p. 57; Order Docket No. 12-0001, 9/19/2012, p. 188) In Docket No. 12-0001, the Commission adopted Staff's proposal to use a short-term debt cost of zero whenever the short-term debt balance for a given calendar year is zero. (Order, Docket No. 12-0001, 9/19/2012, pp. 131-132) This is the same recommendation Staff made in the instant case. (Staff

Ex. 9.0, Attach. A, p. 17) Staff recommends that the Final Order in this proceeding adopt a short-term debt rate of zero percent, given AIC's average 2011 short-term debt balance equals zero, as adopted in Docket No. 12-0001. AIC has indicated that it no longer contests this issue in the instant case in light of the prior Commission Order.

C. Contested Issues

1. Average or Year-End Capital Structure

Staff has explained why an average capital structure is superior to a year-end capital structure for formula ratemaking purposes.[10] (Staff IB, p. 35; Staff Ex. 9.0, Attachment A, pp. 2-9) In the initial formula ratemaking proceedings, the Commission adopted Staff's proposal to use an average capital structure for AIC and Commonwealth Edison Company ("ComEd"), stating Staff's proposed average capital structure more accurately reflects the company's actual capital structure, is consistent with Commission practice and law, and mitigates the risk of manipulation. (Order, Docket No. 12-0001, September 19, 2012, p. 110; Order, Docket No. 11-0721, May 29, 2012, p. 123)

The Company has offered no cogent reason for the Commission to either treat AIC differently than ComEd on this matter or reach a different conclusion in this case than it did in AIC's first formula rate case. Nevertheless, AIC opposes using an average capital structure for formula rates on the basis that an average capital structure is not based on "final or actual data," is precluded by the plain language of the law, and is contrary to HR 1157. (AIC IB, pp. 57-58)

[10] The AIC IB states, "[u]se of average versus year end capital structure (for both inception rates and reconciliation) is another issue that is the subject of the Commission's Order in Docket No. 12-0001." (AIC IB, p. 57) To be clear, neither the Company nor Staff has proposed using a different capital structure for reconciliation than the capital structure used for inception rates.

AIC incorrectly concludes that Staff's proposal produces a capital structure that is not final or actual data because, AIC alleges, "[d]ata concerning the 'actual capital structure' must derived from the same place as most other formula rate inputs: '*final* data based on [the] most recently filed FERC Form 1.'" (AIC IB, p. 57) Yet, AIC does not rely exclusively on year-end FERC Form 1 data. Rather, AIC proposes to calculate a year-end capital structure using ILCC Form 21 data and month-end balances of short-term debt, CWIP and CWIP accruing AFUDC. (AIC IB, p. 57; AIC IB, Appendix A, pp. 13 and 31-33)

AIC's argument that the statute's reference to "actual' capital structure" precludes any calculation other than the Company's end-of year calculation, (AIC IB, p. 58), is patently false. In fact, the Commission's past practices and own rules recognize that the capital structure components may be measured using average balances. (83 Ill. Adm. Code 285.4000(b)) Moreover, the Commission's Order in Docket No. 12-0001 recognized that, although Section 16-108.5(c)(2) of the Act specifies that rates reflect the utility's actual capital structure for the applicable year, it does not specify a measurement methodology for capital structure. (Order, Docket No. 12-0001, 9/19/2012, p. 110) Staff made the same argument in the instant case. (Staff Ex. 9.0, Attach. A, p. 8) Furthermore, the plain language of the statute refers to "calendar year," which *Black's Law Dictionary* defines as, "the period from January 1st through December 31st."

AIC raises the argument that the legislature's intent regarding capital structure in EIMA was made clear with the passage of HR 1157, which stated in part that capital structure using average numbers do not represent final year-end values and is contrary to the statute. This argument makes the erroneous assumption that a resolution of a single chamber of the General Assembly is an expression of the intent of the entire General Assembly. It is not. AIC states that "…any doubts about the legislature's intent were resolved with the recent passage of HR 1157." (AIC RB, p. 58) This statement is supported only by reference to the adoption of HR 1157 by the House of Representatives. The Illinois Constitution vests legislative power in a General Assembly that consists of a Senate and a House elected from 59 Legislative and 118 Representative Districts. (Illinois Constitution 1970, Art. IV, Sec. 1) The action of a single chamber of the General Assembly to pass a resolution does not and cannot represent an expression of the will of the entire Legislature.

Further, HR 1157 was adopted by the one chamber of the General Assembly (the House of Representatives) on August 17, 2012, <u>months</u> after the adoption of the Formula Rate law (October 26, 2011) and the subsequent "trailer bill" (December 30, 2011). It is a well-established principle of law that *post facto* expressions of intent by members of the General Assembly are not properly considered by the Courts, and such matters are inadmissible. (*People v. Chicago Ry. Co*., 270 Ill. 87, 105-106, 110 N.E.2d 386, 393 (1915)) While the Commission may choose to consider the cited resolution in construing the Formula Rate Law, it should give the resolution exactly the amount of weight it deserves—none.

The issue of whether an average or year-end capital structure should be utilized has been litigated and resolved by the actions of the Commission in not only the AIC formula rate case, Docket No. 12-0001, but also the ComEd formula rate case, Docket No. 11-0721. (Order, Docket No. 11-0721, May 29, 2012, p. 123 and Order, Docket No.

12-0001, September 19, 2012, p. 110) Although AIC has recently filed an Application for Rehearing on October 3, 2012, the Final Order in the formula rate case for AIC is the only decision that can be considered determinative in this docket.

For all the foregoing reasons, as well as those set forth in Section VI.C.1. of Staff's Initial Brief, the Commission should adopt Staff's methodology for calculating an average capital structure for formula rates and reject the Company's proposal to determine formula rates using a year-end capital structure.

2. Common Equity Ratio

AIC claims its "calculation of capital structure is legally appropriate based on actual 2011 data and supported by a showing of reasonableness and prudence."[11] (AIC IB, p. 59) AIC bases its claim (1) upon a misinterpretation of Staff's legal position, which is properly set forth in Staff's Initial Brief (Staff IB, pp. 37-39); and (2) upon the erroneous belief that Staff must carry the burden of proof as to the proper capital structure in this proceeding. AIC's argument regarding its capital structure is wrong by all accounts.

The AIC IB begins by stating that, "Staff's legal interpretation of Section 9-230 is incorrect; the law does not automatically require that a 'Participating Utility' adopt its parent's capital structure." (AIC IB, p. 59) This incorrectly implies that Staff's analysis was limited to automatically adopting Ameren Corp.'s ("Ameren") capital structure for AIC. To the contrary, Staff compared AIC's capital structure to that of its parent Ameren and noted that S&P indicates that AIC's regulated operating risk is lower than that of Ameren, which includes significantly riskier generation operations. Given the fact that

[11] In Section VI.C.1 of this reply brief, Staff addresses why the Company's "actual data" argument is erroneous.

AIC has lower operating risk than Ameren, AIC should be able to maintain more financial risk (*i.e.*, have a lower common equity ratio) than Ameren to achieve the same stand-alone credit rating as Ameren. Thus, Staff concluded that Ameren's common equity ratio represents an upper bound for AIC's equity ratio. (Staff Ex. 4.0, p. 10)

Notably, in the instant case, Staff performed the same analysis of AIC's ratemaking capital structure as Staff performed in Docket No. 12-0001. (Order, Docket No. 12-0001, September 19, 2012, pp. 124-125) In that case, the Commission adopted Staff's proposed 51.49% common equity ratio for AIC, stating:

> Section 16-108.5(c)(2) provides that the formula rate approved by the Commission shall "[r]eflect the utility's actual capital structure for the applicable calendar year, excluding goodwill, subject to a determination of prudence and reasonableness consistent with Commission practice and law." As part of its capital structure, AIC presents its common equity ratio of 54.28% while Staff argues for an adjusted common equity ratio of 51.49%...
>
> As for the competing common equity ratios presented by AIC and Staff, the Commission finds merit in Staff's arguments. As noted by Staff, S&P has concluded that AIC's overall operating risk is lower than that of Ameren. The record also reflects that although it continues to have concerns about the regulatory environment in Illinois, Moody's found that the regulatory environment has improved sufficiently to increase AIC's credit rating. Overall, for the reasons contained in the record, the Commission concurs and finds that AIC has lower operating risk than Ameren and now enjoys a more favorable regulatory environment under Public Acts 97-0616 and 97-0646. These facts warrant an adjustment to AIC's 2010 common equity ratio of 54.28%, which represents circumstances as they were prior to Public Acts 97-0616 and 97-0646 and the benefits ensuing to AIC there under. Accordingly, Staff's common equity ratio of 51.49% represents a reasonably adjusted common equity ratio consistent with Commission practice and law, including Section 9-230 of the Act.
>
> (*Id.*, p. 128)

AIC argues, "Staff does not contest AIC's capital structure based upon prudence or reasonable standards…Rather, Staff relies upon Section 9-230 of the Act." (AIC IB, p. 59) A utility does not reach the "prudence and reasonable" determination unless and until the utility's capital structure meets the requirements set forth in Section 9-230 of the Act. (Staff IB, p. 38) Since Section 9-230 absolutely bars, as a matter of law, the adoption of a capital structure that results in increased risk for a utility due to an affiliation with a non-utility coupled with the fact that AIC's capital structure has a higher equity ratio than its parent company despite its lower degree of operating risk, Staff concludes that AIC's capital structure violates the requirements of Section 9-230 of the Act. As such, logic, and controlling case law, dictates that the Company's proposed capital structure is intrinsically neither prudent nor reasonable. (Staff IB, pp. 36-41)

AIC fails to refute Staff's evidence that AIC's capital structure violates Section 9-230 of the Act by providing evidence that AIC meets the requirements set forth in Section 9-230. Rather, AIC attempts to bolster its argument that its capital structure is "legally appropriate" and does not include any incremental risk or increased cost of capital as a direct or indirect result of its affiliation with Ameren by attempting to shift the burden of proof to Staff in demonstrating that "there *must* be a record basis to indicate that the capital structure includes any incremental risk or increased cost of capital which is the direct or indirect result of the public utility's affiliation with unregulated or nonutility companies. (AIC IB, p. 60 *citing Illinois-American Water Co.*, Docket No. 11-0767, Order, p. 79 (Sept. 19, 2012) (IAWC Order; emphasis added)) The Commission made no such conclusion in 11-0767, which would be in direct violation of the fundamental requirement of Section 9-201 that the utility bears the burden of proof in rate cases. 220 ILCS 5/9-201.[12]

In the IAWC Order, the Commission rejected Staff's Section 9-230 position and instead looked back at the proportions of debt and equity in the Illinois American 09-0319 case. (IAWC Order, p. 79) It concluded that it was "appropriate to increase the proportion of each [debt and equity] by one half of the proportion by which the short-term dept proportion was decreased." *Id*. The Commission noted that the record did not indicate one way or another that there was any prohibited incremental risk or increased cost of capital. *Id.* That comment, which is clearly *dicta*,[13] is a far cry from the Commission imposing a new, and unlawful, requirement upon Staff that it *must* carry a burden of proof regarding the record on Section 9-230 issues.

AIC also cites to the IAWC Order to allude to the fact that because Staff did not raise the 9-230 issue in prior proceedings that this somehow makes Staff's argument less accurate or credible. (AIC IB, p. 65) This is merely a red herring designed to distract from Staff's salient points regarding the very real problem with AIC's capital structure. No party is precluded from raising an issue simply because it has not done so in the past.

In the instant case, AIC failed to provide any evidence that AIC's common equity ratio must be higher than Ameren Corp.'s common equity ratio in order for AIC to maintain its current credit rating. Yet, the Company falsely claims, "Staff has presented

[12] Section 9-201 provides in relevant part that: "the burden of proof to establish the justness and reasonableness of the proposed rates or other charges, classifications, contracts, practices, rules or regulations, in whole and in part, shall be upon the utility."

[13] *See* Black's Law Dictionary, Abridged Sixth Ed. (1991), West Publishing Co., St. Paul, Minnesota, which defines "Dicta" as: "Opinions of a judge which do not embody the resolution or determination of the specific case before the court. Expressions in court's opinion which go beyond the facts before court and therefore are individual views of author of opinion and not binding in subsequent cases as legal precedent."

no objective, numerical analysis that reducing the Company's common equity ratio now would not result in a reduction to credit quality, i.e., a ratings downgrade." (Ameren Ex. 12.0, p. 6) In fact, Staff performed a quantitative analysis that shows reducing the Company's common equity ratio to 51% would not cause a credit rating downgrade for AIC.

Specifically, Staff first determined AIC could achieve a 51% common equity ratio by replacing $80 million common equity with long-term debt. Next, Staff evaluated the effect of Ameren Illinois replacing $80 million common equity with $80 million, 6.39% 30-year, BBB-rated utility bonds on the financial risk benchmarks published by Standard & Poor's ("S&P") and Moody's Investors Service ("Moody's").[14] (Staff Ex. 9.0, pp. 4-5) Staff relied upon financial benchmarks that were provided by the Company in response to a Staff data request and calculated in accordance with the S&P and Moody's methodologies. Staff calculated adjusted[15] ratios for S&P's financial risk benchmarks: (1) funds from operations ("FFO") to debt; (2) debt to earnings before interest, taxes, depreciation and amortization ("EBITDA"); and (3) debt to capital. Staff also calculated adjusted ratios for Moody's financial risk benchmarks: (1) cash flow from operations ("CFO Pre-W/C") to debt; (2) CFO Pre-W/C, less dividends, to debt; (3) CFO Pre-W/C, plus interest, to interest expense; and (4) debt to capital. (Staff Ex. 9.0, p. 5)

Staff compared those adjusted ratios to the ranges that S&P and Moody's publish for each of those financial risk benchmark ratios, which vary according the

[14] The current yield on 30-year BBB-rated utility bonds is 4.24%. (Staff Ex. 9.0, footnote 7, citing Citi Research, "Bond Market Roundup," January 8, 2010, p. 16; Citi Research, "Bond Market Round," August 17, 2012, p. 17)

[15] In this context, "adjusted" refers to financial ratios that reflect an $80 million exchange of debt for common equity.

strength of the financial risk benchmark, and found that replacing $80 million common equity with long-term debt would not result in lower implied credit ratings for any of AIC's financial risk benchmarks. (*See* Staff Ex. 9.0, Sch. 9.01 and 9.02.) Thus, Staff concluded that a 51% common equity ratio for the Company would not result in a credit rating downgrade. (Staff Ex. 9.0, pp. 5-6)

AIC argues:

> [Staff's] analysis is flawed in that Ms. Phipps admitted that she cannot know with certainty how a credit ratings agency will actually rate AIC… Mr. Martin concludes that if it were actually to undertake such a transaction, AIC would experience "some degree of deterioration of key credit metrics…"
>
> (AIC IB, pp. 64-65)

Neither Staff nor the Company can guarantee what will happen in the future. Yet, the AIC IB states:

> Mr. Martin advises that "maintaining credit ratios at the strong end of the range…is necessary to offset other factors that put downward pressure on ratings." That downward pressure is a perception of current regulatory environment as being sub-investment grade… As Mr. Martin cautiously advises, "now is not the time to make significant changes to [AIC's] capital structure." He further warns that doing so could put AIC in jeopardy of a downgrade and potentially increase the cost to ratepayers associated with EIMA improvements.
>
> (AIC IB, p. 65)

According to the S&P Business Risk / Financial Risk Matrix, AIC's implied credit rating from S&P is in the A/A- range and that does not change when $80 million of long-term debt replaces $80 million of common equity. (Staff Ex. 9.0, Sch. 9.01) Similarly, AIC's scores for Moody's remain in the investment grade categories with one exception that is unrelated to Staff's assumption regarding AIC's common equity ratio. (Staff Ex. 9.0, Sch. 9.02) As Staff explained in testimony:

> …in 2011, AIC's discretionary dividend payment resulted in a financial risk metric that was in the below investment grade range. Specifically, AIC's retained cash flow ratio (*i.e.*, (CFO Pre-W/C – Dividends) / Debt) fell from the Aa-range in 2010 to the Ba-range in 2011 because AIC's cash flows before dividends fell from $719 million to $493 million, yet its dividend payments increased from $137 million to $330 million. Substituting the 2010 dividend payment of $137 million in the 2011 retained cash flow ratio calculation would have resulted in 2011 retained cash flow ratios that fall in the Baa-range (*i.e.*, 16.4% unadjusted and 15.7% adjusted).
>
> (Staff Ex. 9.0, p. 6, footnote 10)

As is frequently the case, the Company's actions contradict its testimony. That is, AIC opposes adjusting the ratemaking capital structure even though doing so would not result in <u>any</u> of the credit metrics to fall below investment grade, yet AIC made dividend payments that reduced one of Moody's credit metrics to junk rating level.

Staff explained that the implementation of formula rates have affected AIC's credit quality favorably. (Staff IB, p. 37) Specifically, S&P states the new law improves regulatory risk and provides a "streamlined process" for rate setting expected to improve the stability of the utilities' cash flows and ultimately reduce regulatory lag. (Staff Ex. 9.0, Attach C) Similarly, Moody's upgraded AIC's credit rating to Baa2 from Baa3, noting the upgrade "reflects strong, stable cash flow coverage metrics and improved clarity on cost recovery following the passage of formula rate plan legislation in Illinois." (Staff Ex. 4.0, pp. 7-8, citing Moody's Investors Service, "Rating Action: Moody's upgrades Ameren Illinois," June 12, 2012) Moody's also noted that the formula rates plan should result in more timely cost recovery, resilient credit metrics, and better ability to earn returns, while helping to substantially offset lingering concerns about the regulatory framework. (Staff Ex. 4.0, p. 8, citing Moody's Investors Service, "Rating Action: Moody's upgrades Commonwealth Edison's ratings," March 2, 2012, p. 1; Moody's Investors Service, "Credit Opinion: Commonwealth Edison Company," March 5, 2012, pp. 2-3; Moody's Investors Service, "Rating Action: Moody's Downgrades Ameren Genco to Ba2; Places Ameren Illinois on Review for Possible Upgrade," February 29, 2012, p. 1)

Moreover, AIC cannot provide any credit rating statement that supports its assertion that "[t]he risks that AIC's situation pose to Ameren's credit quality may be partially mitigated by the parent's investment in other companies." (Ameren Ex. 12.0, p. 6; Company response to ICC Staff DR RMP 5.02, as provided in Staff Cross. Ex. 5) Although Mr. Martin alleged he was not aware of any impact of the activities of any Ameren affiliate on AIC's cost of capital (Ameren Ex. 12.0, p. 4), S&P expressly states that AIC's affiliation with Ameren Corp's competitive generation businesses have negatively affected AIC's credit rating. Specifically, S&P states:

> Our corporate credit rating on [Ameren Illinois] suffers slightly from the company's affiliation with Ameren's nonrate regulated competitive generation businesses. The competitive businesses' fair business risk profile reflects their ultimate dependence on the market price of electricity, which has recently sharply declined.
>
> (Staff Ex. 9.0, Attach. C)

AIC asserts that Staff's analysis did not consider the two other common rating agencies, Moody's and Fitch. (AIC IB, p. 62) AIC is wrong. As explained previously, in its analysis, Staff adjusted and evaluated Moody's credit rating benchmarks for AIC and Staff identified statements from Moody's regarding AIC's declining operating risk.

AIC asserts further, "…if the common parent is not supporting the unregulated subsidiary, cross-subsidization of risks cannot be found." (AIC IB, p. 63) However, Moody's expressly states that parent company support is important to the maintenance of Ameren Energy Generating Company's ("AmGen") current Ba3 rating. (Staff Cross Ex. 5, Moody's Credit Opinion, "Ameren Energy Generating Company," April 13, 2012, as provided in response to Staff data request RMP 1.02)

The AIC IB states, "Mr. Martin noted that the current debt rating of AIC, while recently upgraded by Moody's remains relatively weak with Standard & Poor's rating AIC one notch above junk bond status, and Moody's only two." (AIC IB, p. 61) The Company's arguments focus exclusively on AIC's issuer ratings of BBB- from S&P and Baa2 from Moody's. This argument is disingenuous on three grounds. First, Mr. Martin's surrebuttal, which AIC cites as the basis for that argument, never described AIC's credit ratings as "weak." In fact, if he had done so, it would have conflicted with the Company response to RMP 5.03, provided just four weeks prior to the filing of Mr. Martin's surrebuttal testimony, which discloses that the Company targets Baa/BBB credit ratings:

> Management believes it is important and in the best interest of the Company's ratepayers for the Company to maintain investment credit ratings within the general Baa/BBB rating level (inclusive of Baa3, Baa2 and Baa1 for Moody's and BBB-, BBB, and BBB+ for S&P's and Fitch. Such ratings will facilitate the Company's access to capital markets on a timely basis, at a reasonable cost and under reasonable terms and conditions.
>
> (Company response to RMP 5.03, August 9, 2012, as provided in Staff Cross Ex. 5)

Either the Company purposely targets a "weak" credit rating, or Ameren does not truly regard credit ratings one notch above junk as "weak."

Second, as the quotation from Standard & Poor's demonstrates, AIC's generating affiliates have negatively affected Standard & Poor's credit rating. Third, AIC's presentation to investors does not even include AIC's issuer rating. It only provides AIC's senior secured rating, which is Baa1/BBB/BBB+[16] (Staff Cross Ex. 5, p. 12, Ameren's March 2012 Investor Meeting [page 38 of original document])) and was recently upgraded to A3 by Moody's. (Tr., September 13, 2012, p. 215) This suggests that the Company regards its secured credit ratings as more important than its issuer credit ratings.

Importantly, despite the higher degree of operating risk for Ameren's merchant generation business vis-à-vis its regulated operations,[17] Ameren Corp. made presentations to all three rating agencies, which show (with one exception[18]) a lower common equity ratio for the Regulated Segments (*i.e.*, AIC and Ameren Missouri) than Merchant Generation in years 2011 – 2016. (Staff Cross Ex. 5, S&P Update, pp. 6, 44-45; Tr. September 13, 2012, pp. 215-216)

Furthermore, AIC alleges, "capital contributions received by the Company from Ameren in 2009 were necessary to strengthen the Company's capital structure and liquidity in the aftermath of the global financial crisis." (Ameren Ex. 12.2, p. 6) The facts

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[16] The Baa1, BBB, and BBB+ senior secured ratings for Ameren Illinois are the ratings from Moody's, S&P, and Fitch, respectively.

[17] As denoted by the S&P business profile score of "Fair" for AmGen, versus "Excellent" for AIC. (Tr., September 13, 2012, p. 216; Staff Ex. 9.0, Sch. 9.01)

[18] The capitalization metrics, presented on pp. 44-45 of the S&P Update included in Staff Cross Ex. 5, are shown for the "Ameren Point of View" and the "Market View." In 2016, the "Ameren Point of View" projects the common equity ratio for the merchant generation business will increase from 51.3% in 2015 to 58.1% in 2016 whereas it projects the common equity ratio for the regulated segments will fall from 51.7% in 2015 to 51.5% in 2016.

indicate otherwise. If strengthening AIC's capital structure was necessary in the aftermath of the global financial crisis then it should have been a greater imperative to strengthen AmGen's weaker capital structure. However, AmGen did not receive any common equity infusion from Ameren "in the aftermath of the global financial crisis." Instead, Ameren Corp. infused common equity into its regulated company while its riskier generation company issued debt. Specifically, in 2009, AIC received a $272 million capital contribution from its parent company and reduced its outstanding indebtedness by $312 million (*i.e.*, repaid $62 million short-term debt, plus $250 million long-term debt). (Staff Cross Ex. 5, p. 6, AIC Cons. Statement of Cash Flows [page 91 in the original document]) At the same time, AIC's unregulated affiliate, AmGen, borrowed $200 million (*i.e.,* issued $249 million long-term debt, and reduced short-term debt by $49 million).[19] (Staff Cross Ex. 5, p. 10, AmGen Cons. Statement of Cash Flows [page 95 in the original document]) As a consequence, by the end of 2010, less risky AIC had a 57% equity ratio whereas riskier AmGen had a 51% equity ratio. (Staff Cross Ex. 5, pp. 5 and 9, Cons. Balance Sheets for AIC and AmGen, respectively [pages 90 and 94, respectively, in the original document]) Clearly, Ameren's 2009 infusion of common equity into AIC constitutes the very form of manipulation of capital structure the Court in *Citizen's Utility Board v. Commerce Commission* ("*CUB*") found to be in contravention of Section 9-230 of the Act, in which higher cost common equity is

[19] Even when retained earnings are included in the comparison, AmGen increased its debt leverage during the global financial crisis. In 2009, AmGen retained $117 million (Staff Cross Ex. 5, p. 11, [numbered page 96 in the original document.]) Thus, during 2009, 63% of AmGen's new capital was debt (i.e., $200 million of debt and $117 million of common equity), which increased AmGen's debt ratio. That same year, AIC retained $143 million in earnings. (Staff Cross Ex. 5, p. 7 [numbered page 92 in the original document.])

added to the capital structure of the rate regulated entity while lower cost debt is used at the unregulated affiliate. (*CUB*, 276 Ill. App. 3d 730, 745(1st Dist. 1995))

For all the foregoing reasons, the Commission should adopt Staff's proposed capital structure for AIC, which includes a 51% equity ratio that is consistent with Commission practice and law, including Section 9-230 of the Act.

3. Common Equity Balance – Purchase Accounting

AIC opposes Staff's proposed purchase accounting adjustment to AIC's common equity balance (AIC IB, pp. 66-68), which would reverse all purchase accounting adjustments reflected in the common equity balance, including goodwill and those income statement purchase accounting adjustments that the Company alleges it paid out in dividends. (Staff IB, pp. 41-43)

AIC claims, "[t]he issue presented in this docket is either identical or nearly identical to those presented in the 11-0282 and 12-0001 dockets." (AIC IB, p. 67) To be clear, in Docket No. 11-0282, Staff's primary recommendation involved reducing the common equity balance by the amount of goodwill rather than the amount of purchase accounting adjustments, including goodwill. (Final Order, Docket No. 11-0282, January 10, 2012, p. 51) In Docket No. 12-0001, Staff recommended subtracting all purchase accounting adjustments, including goodwill, from the common equity balance, in recognition of the Commission's determination in Docket No. 11-0282 that purchase accounting and goodwill are intertwined. (Order, Docket No. 11-0282, January 10, 2012, p. 54)

AIC alleges that Staff's adjustment does not comply with the Commission's Order in Docket No. 04-0294 and seeks to remove amounts already removed from the equity balance. (AIC IB, p. 66) To the contrary, AIC failed to follow the Commission's Order in Docket No. 04-0294 by claiming to "effectively eliminated" approximately $100 million of net income related purchase accounting adjustments by paying cash dividends rather than reversing all purchase accounting adjustments, as required by the Docket No. 04-0294 Order. (Staff IB, p. 41-43) According to Company witness Mr. Stafford:

> To the extent changes to net income have resulted from purchase accounting transactions, then such adjustments did flow through retained earnings and, prior to common dividend payments, remained in retained earnings. However, the premise for Ms. Phipps adjustment is wrong… simply because retained earnings are impacted by purchase accounting adjustments is not the determinative factor, but whether such earnings are still in fact "retained" by the utility included in the Company's common equity balance. The problem with Ms. Phipps' approach is that she reverses purchase accounting adjustments that are no longer reflected in retained earnings, and thus are not included in the common equity balance she is adjusting.
>
> (Ameren Ex. 11.0R, pp. 9-10)

The assumption underlying AIC's adjustment is that the Commission cannot adjust what has been "effectively eliminated" through the payment of dividends. (AIC IB, p. 66; Ameren Ex. 19.0R, p. 10; Staff Cross Ex. 6, p. 2) Staff contends it will be necessary to remove net income related purchase accounting adjustments from AIC's common equity balance until all purchase accounting adjustments that flow through retained earnings are fully amortized. This proposed regulatory treatment would be identical to the purchase accounting adjustments recorded to Account 114, which also need to be deducted from the Company's common equity balance until they are fully amortized. (Staff Ex. 9.0, p. 4)

Furthermore, AIC relied upon an arbitrary and unfounded methodology for determining whether cash dividends were "paid" from accumulated earnings from purchase accounting net income ("PA net income") or accumulated earnings from non-purchase accounting net income ("non-PA net income"). (Staff Cross Ex. 6, pp. 1-3 and 7) If AIC had allocated 2007 and 2008 dividend payments in the same manner it allocated 2005 and 2006 dividend payments, then AIC's adjustment would have been closer to Staff's proposed adjustment. That is, unlike preceding years, AIC "paid" dividends from PA net income first during 2007 and 2008. (Staff Cross Ex. 6, p. 7, notes (3) and (4)) AIC's methodology inflated its common equity balance for ratemaking purposes. Furthermore, even though AIC may not have violated any accounting rules, its methodology is not dictated by accounting rules either. (Order, Docket No. 12-0001, September 19, 2012, p. 113)

In any case, the purchase accounting adjustments are not reversed because they violate accounting rules. No one argued that AIC violated accounting rules when it applied purchase accounting rules to its financial statements at the time that Ameren acquired Illinois Power. Nonetheless, in Docket No. 04-0294, the Commission ordered Illinois Power to reverse those purchase accounting adjustments for ratemaking purposes. (Order, Docket No. 04-0294, 9/22/2004, Appendix A, p. 3) The Commission did not provide Illinois Power an alternative to reversing its purchase accounting adjustments such as common dividend "offsets."

In summary, reconciling the Company's claim that it eliminated purchase accounting adjustments through the payment of cash dividends, (AIC IB, p. 66; Ameren Ex. 19.0R, p. 10; Staff Cross Ex. 6, p. 2), with the economic reality that purchase accounting adjustments do not generate cash that can be paid out as dividends to investors, (Staff Ex. 9.0, Attach A, pp. 14-15), would be impossible if not for the

Company's misinterpretation of Section 7-103 of the Act. That is, AIC argues that it could not have paid those cash dividends if not for purchase accounting because a positive retained earnings is supposedly a legal pre-condition for the payment of dividends. (Order Docket No. 12-0001, September 19, 2012, pp. 113 and 118) The Staff IB explains the errors in AIC's position, including the Company's misinterpretation of Section 7-103 of the Act. (Staff IB, pp. 41-43) For all the foregoing reasons, Staff recommends the Commission adopt its proposed adjustment to remove all purchase accounting adjustments, including goodwill, from the Company's common equity balance, which is based on an interpretation of Section 7-103 of the Act that is consistent with prior Commission decisions.

4. Balance and Embedded Cost of Long-Term Debt

In AIC's first formula rate case, Docket No. 12-0001, and ComEd's first formula rate case, Docket No. 11-0721, the Commission adopted Staff's calculation of the average embedded cost of long-term debt for formula rates. (Order, Docket No. 12-0001, September 19, 2012, p. 129; Order, Docket No. 11-0721, May 29, 2012, p. 138) In this case, the Commission should also adopt Staff's calculation of AIC's embedded cost of long-term debt for the reasons set forth in Sections VI.C.1 and VI.C.4 of Staff's Initial Brief (Staff IB, pp. 35 and 44) and Section V1.C.1. of this Reply Brief regarding the reasons an average capital structure is superior to a year-end capital structure for formula rates.

5. Balance and Embedded Cost of Preferred Stock

In AIC's first formula rate case, Docket No. 12-0001, the Commission adopted Staff's calculation of the average embedded cost of preferred stock for formula rates. (Order, Docket No. 12-0001, September 19, 2012, p. 129) In this case, the Commission should also adopt Staff's calculation of AIC's embedded cost of preferred stock for the reasons set forth in Sections VI.C.1 and VI.C.5 of Staff's Initial Brief (Staff IB, pp. 35 and 44) and Section V1.C.1. of this Reply Brief regarding the reasons an average capital structure is superior to a year-end capital structure for formula rates.

VII. COST OF SERVICE AND RATE DESIGN

A. Uncontested or Resolved Issues

1. Consistency with Docket No. 12-0001

VIII. FORMULA RATE TARIFF-- RECONCILATION

A. Uncontested or Resolved Reconciliation Issues

B. Contested Reconciliation Issues

On September 19, 2012, the Commission issued its Final Order in Docket No. 12-0001, establishing the structure and protocols for AIC's performance based rate tariff (Rate MAP-P), pursuant to Section 16-108.5 of the Public Utilities Act ("Act"). (220 ILCS 5/16-108.5 *et seq*) This annual update proceeding, initiated pursuant to Section 16-108.5(d), has but one purpose: to update the cost inputs to the performance-based formula rate for the applicable rate year and the corresponding new charges. (220 ILCS 5/16-108.5(d)) It is clear that any arguments as to the structure or protocols of Rate MAP-P set in Docket No. 12-0001 should be disregarded as they are not applicable to this proceeding. In fact, Section 16-108.5(d) explicitly states that the Commission is not to consider such issues in its determination in this proceeding:

> The Commission shall apply the same evidentiary standards, including, but not limited to, those concerning the prudence and reasonableness of the costs incurred by the utility, in the hearing as it would apply in a hearing to review a filing for a general increase in rates under Article IX of this Act. *The Commission shall not, however, have the authority in a proceeding under this subsection (d) to consider or order any changes to the structure or protocols of the performance-based formula rate approved pursuant to subsection (c) of this Section.*
>
> 220 ILCS 5/16-108.5(d)(emphasis added)

AIC's own witness, Craig Nelson acknowledged this fact in direct testimony. (AIC Ex. 9.0, pp. 2-3) Whether the record in this case is different from that in Docket No. 12-0001 is irrelevant (AIC IB, p. 69), because these issues have been resolved in the initial formula rate proceeding and cannot be re-litigated each year.

The decision in Docket No.12-0001 is not, as Ameren argues, a temporary one subject to further argument in this proceeding. (*Id*.) The order is exactly as described, *final.* To date, the Commission has not granted rehearing on any issue, let alone (1) Average or Year-End Reconciliation Rate Base; (2) Interest Rate on Under/Over Reconciliation Balances; or (3) Average or Year-End Capital Structure.[20]

Rehearing on these three identical issues in Commonwealth Edison Company's formula rate proceeding is also final. (Order on Rehearing, Docket No. 11-0721, October 3, 2012) The Commission confirmed that the appropriate reconciliation rate base was an average rate base, the appropriate interest rate on over/under reconciliation balances is a short-term debt cost rate, and that an average capital structure should be used for purposes of the formula rate reconciliation. (*Id*.) Particularly with reference to the use of year-end versus average data, the Commission

[20] AIC filed its Application for Rehearing in Docket No. 12-0001 on October 4, 2011. It is unclear when or if the Commission will grant rehearing on any of the 5 issues articulated in the Application.

noted that consistency between utilities in formula rate proceedings was both an important and motivating factor behind its decisions:

> In Docket No. 12-0001, the Commission strove to maximize, where appropriate, the consistency between the findings in that case and in this case. On the issue of average versus year-end data, as discussed further below, the Commission finds it appropriate that there be consistency between the two utilities in Illinois that are filing tariffs under the EIMA formula rate option.
> (*Id*, p. 18)

In light of this Order on Rehearing, it belies common sense to argue that the Commission should come to a different conclusion on these issues in the current proceeding, and, as 16-108.5(d) plainly states, the Commission does not have the authority to do so.

1. Average or Year-End Reconciliation Rate Base

2. Interest Rate on Under/Over Reconciliation Balances

3. Average or Year-End Capital Structure

For the same reasons that Staff supports an average capital structure for formula rate proceedings, as set forth in Staff's Initial Brief, on p. 35, Section VI.C.1 in this Reply Brief, the Commission's Order in Docket No. 12-0001, and the Commission's Order in Docket No. 11-0721, the Commission should adopt an average capital structure for reconciliation purposes.

IX. OTHER

A. Resolved or Uncontested Issues

1. Original Cost Determination

2. Uncollectibles Expense

3. Coordination with Docket No. 12-0001

4. AFUDC Rate — Plant Balances

5. Reporting of Plant Additions Pursuant to Section 16-108.5(b)

6. Income Taxes—Interest Synchronization

7. Gross Revenue Conversion Factor

X. CONCLUSION

WHEREFORE, for all of the following reasons, Staff respectfully requests that the Commission's order in this proceeding reflect all of Staff's recommendations regarding AIC's request for approval of its updated cost inputs for its Modernization Action Plan - Pricing tariff, Rate MAP-P and corresponding new charges.

October 11, 2012 Respectfully submitted,

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