

CUB/IEC Exhibit 2.0

**STATE OF ILLINOIS  
ILLINOIS COMMERCE COMMISSION**

\_\_\_\_\_)  
Ameren Illinois Company )  
d/b/a Ameren Illinois )  
)  
Rate MAP-P Modernization Action )  
Plan - Pricing Annual Update Filing. )  
\_\_\_\_\_)

**Docket No. 14-0317**

Rebuttal Testimony of

**Michael P. Gorman**

On behalf of

**Citizens Utility Board  
and Illinois Industrial Energy Consumers**

August 28, 2014



59 its regulated operations in Illinois. This increased profit also increases its cash flows,  
60 and is a direct benefit to its investors. Therefore, the need for an increase in  
61 materials and supply inventory should be explained and justified as prudent and  
62 reasonable, along with all other costs included in the formula rate process, in order to  
63 ensure that the rates charged to retail customers reflect only its actual prudent and  
64 reasonable cost of service.

65 **Q ABSENT SUCH JUSTIFICATION, DO YOU CONTINUE TO SUPPORT AN**  
66 **ADJUSTMENT TO THE LEVEL OF MATERIALS AND SUPPLIES INCLUDED IN**  
67 **THE FORMULA RATES RESULTING FROM THIS CASE?**

68 A Yes. Without this justification, Ameren Illinois has not shown that its level of materials  
69 and supplies is prudent or reasonable. Therefore, I support an adjustment to reflect  
70 an average of the materials and supplies balances from 2010 through 2013. This  
71 adjustment reduces the materials and supplies rate base balance included in the  
72 calculation of formula rates and the resulting revenue requirement in this case by  
73 \$6.6 million and \$1.7 million, respectively.

74 **RECONCILIATION BALANCE INTEREST**

75 **Q PLEASE EXPLAIN THIS PORTION OF YOUR TESTIMONY.**

76 A This portion of my rebuttal testimony will address the issue of the appropriate level of  
77 interest associated with the reconciliation balance. I will respond to the rebuttal  
78 testimonies of Ameren Illinois witnesses Ronald D. Stafford (Ameren Ex. 13.0 (Rev.)),  
79 James C. Blessing (Ameren Ex. 18.0) and James I. Warren (Ameren Ex. 15.0 (Rev.))  
80 regarding this issue.

81 **Q PLEASE SUMMARIZE MR. STAFFORD'S TESTIMONY REGARDING THIS ISSUE.**

82 A In his rebuttal testimony at lines 134 through 144, Mr. Stafford discusses my  
83 recommendation to reduce the amount of reconciliation balance interest through a  
84 modification to formula rate schedule FR Sch. A-4 and his understanding that  
85 changes to formula rate schedules and appendices cannot be made in the current  
86 proceeding, an annual formula rate update. He further opines that changes to  
87 formula rate schedules and appendices can only be made in a separate  
88 Section 9-201 proceeding before the Commission (pursuant to Section 16-108.5 of  
89 the Public Utilities Act, the "Formula Rate Law").

90 **Q IS MR. STAFFORD'S UNDERSTANDING OF THE NEED FOR A SECTION 9-201**  
91 **PROCEEDING PURSUANT TO THE FORMULA RATE LAW CORRECT?**

92 A No. I understand that in its Final Order dated August 19, 2014 in Consolidated  
93 Docket Nos. 13-0501 and 13-0517 at page 26, the Commission stated that a Section  
94 9-201 filing is not necessary for changes to formula rate schedules, appendices, or  
95 workpapers, other than the specific formula rate schedules FR A-1 and FR A-1 -  
96 REC.

97 **Q ARE YOU RECOMMENDING ANY CHANGES TO FORMULA RATE SCHEDULES**  
98 **FR A-1 AND/OR FR A-1 - REC?**

99 A No. My recommendation adjusts the amount of reconciliation interest on a  
100 workpaper, WP 23, which flows to line 30a of formula rate schedule FR A-4.  
101 Therefore, my adjustment is to a data input to the formula rate, and is not an  
102 adjustment to the formula rate.

103                   As I previously stated in my direct testimony in this proceeding at page 7, the  
104                   adjustment does not disturb the formula rate schedules FR A-1 or FR A-1 - REC.  
105                   Therefore, based on my layperson's understanding of the Commission's Final Order  
106                   in Consolidated Docket Nos. 13-0501 and 13-0517, the adjustment I am  
107                   recommending to the amount of interest on the reconciliation balance can be  
108                   considered in this proceeding.

109    **Q       PLEASE SUMMARIZE MR. BLESSING'S TESTIMONY REGARDING THIS ISSUE.**

110    A       I understand that the main focus of Mr. Blessing's testimony with regard to my  
111                   recommendation is that the specific language in the Formula Rate Law, either as  
112                   originally passed or later amended by the legislature, does not address a reduction to  
113                   the reconciliation balance.

114    **Q       WHAT IS YOUR RESPONSE?**

115    A       I believe the Commission can and should use its discretion to interpret the Formula  
116                   Rate Law, when the plain meaning of the language is called into question and parties  
117                   present a sound ratemaking position on an issue.

118    **Q       HAS THE COMMISSION PREVIOUSLY EXPRESSED ITS OPINION REGARDING**  
119                   **THE CLARITY OF THE FORMULA RATE LAW LANGUAGE AND THE VALUE OF**  
120                   **THE POSITION THAT RECONCILIATION BALANCE INTEREST SHOULD BE**  
121                   **REDUCED TO REFLECT ASSOCIATED TAX BENEFITS?**

122    A       Yes. In its Interim Order dated November 26, 2013 in Consolidated Docket Nos.  
123                   13-0501 and 13-0517 at page 26 relating to this issue, the Commission disagreed  
124                   with Ameren Illinois regarding the clarity of the language in the Formula Rate Law.

125 The Commission also found merit in the AG's position in this case, which conformed  
126 to Generally Accepted Accounting Principles and would capture deferred tax benefits.  
127 In addition, the Commission stated that the position is likely a more accurate  
128 accounting for all of the economic impacts caused by revenue requirement  
129 reconciliation.

130 **Q IS THE RECOGNITION OF DEFERRED INCOME TAX BENEFITS IN FORMULA**  
131 **RATE PROCEEDINGS SPECIFICALLY DISCUSSED IN THE FORMULA RATE**  
132 **LAW?**

133 A Not exactly. The netting of deferred tax benefits with the pension asset is the only  
134 specific reference to Accumulated Deferred Income Taxes ("ADIT") in the Formula  
135 Rate Law. As a result, other examples where ADIT in formula ratemaking is  
136 recognized, such as the reduction of rate base for ADIT, must be the result of the  
137 Commission's interpretation of the Formula Rate Law. Clearly, the Commission must  
138 make reasonable interpretations in order to effectively implement the formula rate.  
139 Not all ratemaking aspects of developing a utility revenue requirement are explicitly  
140 defined by the Formula Rate Law.

141 **Q HAS AMEREN ILLINOIS MADE RATEMAKING ADJUSTMENTS WHICH ARE NOT**  
142 **SPECIFICALLY REFERENCED IN THE FORMULA RATE LAW?**

143 A Yes. Ameren Illinois has adjusted the amount recorded in the Federal Energy  
144 Regulatory Commission ("FERC") Form 1 for 2013, to recognize cash payments for  
145 injuries and damages. Although this adjustment was not opposed by other parties to  
146 this proceeding, I do not believe this type of ratemaking adjustment is specifically  
147 contemplated by the Formula Rate Law. Recognizing cash payments for injuries and

148 damages increases Ameren Illinois' expenses and its formula rate revenue  
149 requirement. If the Commission can make interpretations that increase revenue  
150 requirement, it would be balanced to also allow it to make reasonable and accurate  
151 interpretations of cost of service that decrease revenue requirements.

152 **Q PLEASE SUMMARIZE MR. WARREN'S TESTIMONY REGARDING THIS ISSUE.**

153 A Mr. Warren describes two methods, which he refers to as models, for calculating  
154 interest on the reconciliation balance. He has labeled his two models as the  
155 "prescribed interest" model and the "cost-based" model and his testimony describes  
156 the two models according to how each model calculates the interest for the  
157 reconciliation balance.

158 **Q HOW DOES MR. WARREN DESCRIBE EACH OF THESE MODELS?**

159 A Mr. Warren first compares the prescribed interest model as similar to the process of a  
160 bank charging interest on a loan balance. According to this model, Mr. Warren  
161 calculates interest by multiplying a rate by the reconciliation balance.

162 Second, Mr. Warren compares the cost-based model to a conventional  
163 regulatory calculation. According to the cost-based model, the reconciliation balance  
164 is reduced by accumulated tax benefits before being multiplied by a carrying charge  
165 rate. However, Mr. Warren assumes the carrying charge rate is based on 100%  
166 common equity capital, and has proposed to gross-up the common equity carrying  
167 charge rate for income taxes.

168 **Q ARE THESE TWO MODELS THE ONLY METHODS APPLICABLE TO THE**  
169 **CALCULATION OF INTEREST ON THE RECONCILIATION BALANCE?**

170 A No. Mr. Warren seeks to establish that his two models are the only ones applicable  
171 to the calculation of interest on the reconciliation balance. These two models are not  
172 specifically described in the Formula Rate Law (220 ILCS 5/16-108.5), and by limiting  
173 the calculation of interest on the reconciliation balance to only these two models,  
174 Mr. Warren is able to reject any method that does not fit into the parameters he  
175 proposes to establish. The method I discuss in my direct testimony produces a level  
176 of interest on the reconciliation balance that fully recovers Ameren Illinois' cost of  
177 carrying the reconciliation balance.

178 **Q DOES YOUR METHOD OF CALCULATING INTEREST MORE ACCURATELY**  
179 **MEASURE AMEREN ILLINOIS' ACTUAL INTEREST EXPENSE ON THE**  
180 **RECONCILIATION BALANCE?**

181 A Yes. The Formula Rate Law clearly states that "interest" is being applied to the  
182 reconciliation balance. Although it is my understanding that the rate of interest is  
183 required by the Formula Rate Law to be equal to the weighted average cost of capital  
184 ("WACC"), it is not a rate of return, and it is my further understanding it is not referred  
185 to as such in the statute. It is simply the "interest" rate to be used as a carrying  
186 charge rate on the reconciliation balance. Interest is tax deductible, and should not  
187 be factored-up for income taxes as suggested by Mr. Warren's second model.

188 The reconciliation balance, to which this carrying charge rate should be  
189 applied, must be examined to establish the amount of Ameren Illinois' increased  
190 interest cost. In Ameren Illinois' case, the reconciliation balance is positive, indicating  
191 that the cost of service was higher than the level reflected in rates. As I discussed in

192 my direct testimony, these higher costs would result in less taxable income and a  
193 reduction in income taxes. This tax benefit results in a lower out-of-pocket income tax  
194 cost associated with the reconciliation balance. A reconciliation balance, net of tax  
195 savings, reflects the amount that Ameren Illinois must use its capital to carry and  
196 which an interest cost will be incurred it recovers the reconciliation balance from  
197 customers.

198 **Q DO YOU BELIEVE THE COMMISSION HAS ACCEPTED THE “PRESCRIBED**  
199 **INTEREST” MODEL?**

200 A No. In its Interim Order dated November 26, 2013 in Consolidated Docket Nos. 13-  
201 0501 and 13-0517 at page 26, the Commission stated the following with regard to the  
202 issue of reducing the amount of interest on the reconciliation balance:

This approach conforms to GAAP, would capture deferred tax benefits,  
and is likely a more accurate accounting for all of the economic  
impacts caused by revenue requirement reconciliation.

203 **Q IS YOUR PROPOSAL CONSISTENT WITH THE COMMISSION’S VIEW AS**  
204 **STATED ABOVE?**

205 A Yes. My proposal reflects a reduction of the carrying charge interest expense on the  
206 reconciliation balance in recognition of the associated tax benefits on the  
207 reconciliation balance.

208 **Q DID THE COMMISSION REJECT A REDUCTION TO THE RECONCILIATION**  
209 **BALANCE FOR ADIT, PRIOR TO THE CALCULATION OF INTEREST, IN THE**  
210 **DETERMINATION OF THE 2013 FORMULA RATE?**

211 A The Commission said that although the Formula Rate Law did not prohibit or require  
212 such accounting treatment, it was difficult to support an interpretation that read into  
213 the statute exceptions, limitations, or conditions the legislature did not express.

214 As I discuss above, the specific inclusion of ADIT is only referenced in the  
215 Formula Rate Law with regard to calculating the pension asset. All other recognition  
216 of ADIT in formula ratemaking had to rely on Commission interpretation, since there  
217 was no specific wording in the Formula Rate Law that directed its recognition.

218 **Q ON PAGE 10 OF HIS REBUTTAL, MR. WARREN STATES THAT INCOME TAXES**  
219 **ARE ALREADY REFLECTED IN THE AMOUNT OF THE RECONCILIATION**  
220 **BALANCE. IS THIS CORRECT?**

221 A Yes. Approximately \$24.7 million of income taxes are included in the approximately  
222 \$60.0 million reconciliation balance, before interest. These are taxes which were not  
223 paid in 2013 and will not be incurred until the reconciliation revenue is billed to  
224 customers in 2015. This is the amount by which the reconciliation balance should be  
225 reduced prior to the application of the interest rate. Ameren Illinois should not be  
226 allowed to collect a carrying cost on taxes that have not yet been paid, and are not  
227 paid until the reconciliation balance is collected from customers.

228 **Q DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

229 A Yes, it does.