AMERENUE DIRECT TESTIMONY

EXECUTIVE SUMMARIES

MPSC CASE NO. GR-2007-0003

JULY 7, 2006

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EXECUTIVE SUMMARY

Richard Mark

Senior Vice President of Missouri Energy Delivery

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AmerenUE has made a concerted effort to improve the service it provides to its customers. These efforts have included improvements at its call centers, upgrades to its billing system and the expansion of the options available to customers on the Company's website, Ameren.com.

AmerenUE routinely measures customer satisfaction by subscribing to various surveys from outside, independent companies such as J.D. Power. AmerenUE also conducts its own surveys. The results of these surveys show that the Company provides excellent customer service. AmerenUE's internal survey found 90% of AmerenUE customers rated their overall experience with the Company as either meeting expectations or above expectations and J.D. Power recently awarded AmerenUE's customer contact centers with the JD Power and Associates certification for providing "An Outstanding Customer Service Experience."

AmerenUE has also made significant contributions to various low income assistance and energy efficiency programs, including $8 million in contributions to the Dollar More Program and approximately $750,000 in contributions for weatherization and efficiency programs, including programs to provide assistance in paying bills in Scott and Stoddard Counties, programs to assist in the replacement of inefficient natural gas residential furnaces and thermostats. AmerenUE is committed to finding ways to assist our customers who are in need as well as helping all customers conserve energy. The Company will work collaboratively with the Commission and other key stakeholders to continue current low-income energy assistance programs and energy conservation programs as appropriate, as well as to develop new programs where beneficial.

EXECUTIVE SUMMARY

SCOTT A. GLAESER

Vice President of Gas Supply and System Control

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My testimony is focused on three areas. First, I propose to consolidate AmerenUE's four Purchased Gas Adjustment (PGA) areas into a single rate mechanism. The primary purpose of the single PGA rate is to provide all of our customers with the benefits of a single PGA which is more stable and less susceptible to market price volatility and spikes. The single PGA will bring the commodity price hedging benefits of a large system to all customers, regardless of their location or the size of the distribution system that serves them. There are no direct financial benefits for AmerenUE from the single PGA rate, but it should provide higher customer satisfaction and less customer confusion. The historic factors that created AmerenUE's four PGA rate areas are no longer relevant in today's gas industry and no longer represent the primary drivers of gas supply costs within the PGA rates. In fact, the rate differentials between the three interstate pipelines that serve AmerenUE are relatively insignificant and completely over shadowed by hourly gas price volatility in today's constrained gas markets. The ability of all of our distribution systems to equally access storage, a fundamental resource in managing price volatility, on any interstate pipeline will be enhanced by a single PGA.

Second, I am proposing revisions to tariff provisions which address Critical Day definition, Unauthorized Gas Usage, and penalties. These changes more clearly define in its tariffs the operating conditions that create a Critical Day on AmerenUE's distribution system(s) and increase the penalties that are charged for unauthorized system gas taken by transportation and interruptible sales customers during these Critical Day periods. This authorized taking of system gas is detrimental to the operation and integrity of the system during Critical Day periods.

Finally, I am proposing changes to the process under which a transportation customer may request a return to the sales function. These changes will give AmerenUE the authority to determine if the Company has sufficient gas supply resources, storage capacity, and transportation capacity to support the transportation customer wishing to return to sales service. I propose this change because interstate and intrastate pipeline capacity markets have become more constrained and AmerenUE may not have incremental firm transportation capacity available to serve transportation customers wishing to return to the sales function. In the event that AmerenUE has insufficient capacity in its existing portfolio to serve a customer wishing to return to sales service, then AmerenUE would have to acquire new incremental capacity from the upstream interstate or intrastate pipeline to serve the customer's demand requirements. AmerenUE simply cannot serve the customer under the sales function if the firm capacity to meet the customer's demand is not available. It is important for AmerenUE to be able to control migration from transportation service to sales service in order to maintain the integrity of the gas supply resources supporting the distribution systems.

EXECUTIVE SUMMARY

Steve Colyer

Manager, Gas Technical Services

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AmerenUE's gas system continues to grow as evidenced by the addition of approximately 215 miles of polyethylene mains and over 10,000 new service lines, over the past three years, to serve new customers. AmerenUE also continues to complete its replacement of cast iron mains and service lines pursuant to replacement plans on file with the Commission. The additional mains, service lines, the replacement programs, and other system upgrades have resulted in capital expenditures over the last three years of more than $40 million, which include ISRS (Infrastructure System Replacement Surcharge) qualifying expenditures which, by December 31, 2006, will meet or exceed the Company's ISRS qualifying expenditure commitment previously made to the Commission. While the Company is not seeking to establish an ISRS in this case, the Company will have sufficient qualifying ISRS investments by 2007 or 2008 and would expect to request an ISRS mechanism at that time.

EXECUTIVE SUMMARY

Gary S. Weiss

Manager of Regulatory Accounting for Ameren Services Company

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The purpose of my testimony is to present the Company's revenue requirement recommendation for its Missouri gas operations. Based on the Company's revenue requirement, a $10,853,000 rate increase under traditional ratemaking is justified.

The Company's revenue requirement is based on a test year consisting of the twelve months ended June 30, 2006, utilizing nine months of actual and three months of forecasted information, with certain known and measurable items updated through September 30, 2006. The three months of forecasted information will be updated with actual data once it becomes available, including the filing of supplemental direct testimony on or before September 30, 2006 supporting that updated information. The Company's rate base is updated through December 31, 2006 to reflect all additions to plant in service except for new business additions. In addition, the remaining infrastructure investments through December 31, 2006 are included as these projects were included in the commitment made by AmerenUE in the Stipulation and Agreement in Case No. GR-2003-0517. The revenues have been adjusted to reflect normal weather. The revenues and expenses related to purchased gas have been eliminated as this case only applies to an increase in the base rates. The remaining operating expenses have been adjusted to reflect the 2006 wage and salary increases, incentive compensation expense has been reduced to the annualized year 2006 target level, pension expense and other employee benefits have been adjusted to reflect the

2006 level annualized and a three-year amortization of the expenses incurred to prepare and litigate this rate increase filing has been included.

The depreciation expense has been decreased to reflect proposed depreciation rates. The proposed depreciation rates are applied to the depreciable plant balances at June 30, 2006 as well as to the additions to plant through December 31, 2006. The testimony of Company witness John F. Wiedmayer provides support for the proposed depreciation rates. Taxes other than income taxes have been adjusted to reflect the increase in F.I.C.A. tax related to the wage and salary increases. Finally, the Company's revenue requirement is based on an 11.50% return on common equity (see the testimony of Company witnesses Kathleen C. McShane and James H. Vander Weide). Reflecting the above items, the Company's Missouri gas operations’ revenue requirement after reflecting an increase in uncollectible accounts is $70,195,000. The Company’s Missouri gas revenue requirement is $10,853,000 greater than the current operating revenues.

EXECUTIVE SUMMARY

Kathleen C. McShane

Senior Consultant and Executive Vice President of
Foster Associates, Inc.

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I have been asked to render an opinion on the fair rate of return on equity that would be applicable to the gas operations of Union Electric Company d/b/a AmerenUE. My analysis and recommendation took into account the following considerations:

(1) The allowed return on equity for AmerenUE's gas operations should reflect the risk profile and cost of equity of comparable gas distribution utilities so as to provide "a return commensurate with returns in other enterprises with corresponding risks." A sample of natural gas distribution utilities (LDCs) serves as the comparable group for AmerenUE's gas operations.

(2) In arriving at a recommended return, no single test result should be given exclusive weight. Each of the various tests employed provides a different perspective on a fair return. Each test has its own strengths and weaknesses, which vary with both the business cycle and stock market conditions. In the end, regardless of the insight that may be added by any individual test, the governing principles from the *Bluefield* and *Hope* decisions of the United States Supreme Court, as the Commission has emphasized, "require[] a *comparative method*, based on the quantification of risk" in determining a fair rate of return on equity.

(3) The discounted cash flow ("DCF") and the risk premium tests are market-related tests for measuring the cost of attracting capital by reference to market values. By

contrast, the comparable earnings test, which reflects returns on book equity, directly addresses the fairness standard as enunciated in the *Bluefield* and *Hope* decisions.

(4) For the purposes of determining a fair return on equity for a utility, a critical factor that needs to be recognized is that the cost of capital is determined in the capital markets. The cost of capital estimates reflect the market value of the firm's capital, both debt and equity. While the DCF and risk premium tests estimate the return required on the market value of common equity, regulatory convention applies that return to the book value of the assets included in rate base. The determination of a fair return on book equity needs to recognize that distinction and the resulting differences in financial risk.

(5) In principle, the comparable earnings test is most compatible with regulation on an original cost book value rate base. For purposes of this testimony, I have used the comparable earnings test results to demonstrate the reasonableness of the recommended return in relation to the level of returns being earned by unregulated non-utility companies with risks similar to gas utilities.

(6) The results of the DCF and risk premium tests used to estimate a fair return for AmerenUE's gas operations, as well as my recommendation, are summarized below.

Table 1

	Range	**Average**
Discounted Cash Flow	8.8-10.2%	9.5%
Capital Asset Pricing Model	11.0-11.5%	11.25%
Achieved Utility Risk Premiums	10.75-11.75%	11.25%
DCF-Based Risk Premium	9.8-10.3%	10.0%
Average of All Cost of Equity Methods		10.5%
Cost of Equity Reflecting Higher Financial Risk of AmerenUE Filed Capital Structure		11.5%

The tests indicate that the required equity return is in the range of 9.5% (DCF) to 11.5% (CAPM). Based on all four tests, the indicated cost of equity as applied to the comparable gas utilities is approximately 10.5%.

The proxy LDC sample's market value common equity ratio is 65%. The allowed return on equity will be applied to AmerenUE's book value common equity ratio of 52%. The difference in financial risk between a market value common equity ratio of 65% and AmerenUE's book value common equity ratio of 52% requires an increase in the equity return requirement from 10.5% to a range of 11.1% to 11.9%. I recommend that the allowed return on equity for AmerenUE's Missouri gas operations be set at the mid-point of the range, that is, at 11.5%.

EXECUTIVE SUMMARY

LEE R. NICKLOY

Director – Corporate Finance and Assistant Treasurer

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The purpose of my testimony is to recommend an overall fair rate of return for AmerenUE's gas utility business. I determine AmerenUE's capital structure, embedded cost of long-term debt and embedded cost of preferred stock. I also calculate the overall fair rate of return applied to rate base which is utilized in AmerenUE's filing in this case. I do so by using the fair rate of return applicable to the common equity component of AmerenUE's capital structure as developed by AmerenUE witness Kathleen McShane in her direct testimony submitted in this case.

Ms. McShane develops and supports a fair return on common equity for AmerenUE's gas utility operations in the range of 11.10% – 11.90% with a recommended cost of equity for AmerenUE of 11.50%. For purposes of determining the overall fair rate of return for AmerenUE in this proceeding, I used Ms. McShane's recommendation, 11.50%, as the Company's cost of common equity.

Using the capital structure (45.420% long-term debt, 0.099% short-term debt, 2.040% preferred stock and 52.441% common equity) and embedded costs of long-term debt (5.427%), short-term debt (5.11%) and preferred stock (5.189%), as shown on the various Schedules attached to my testimony, along with the cost of common equity of 11.50% for AmerenUE developed by Ms. McShane, I derive an overall fair rate of return for AmerenUE of 8.607%.

EXECUTIVE SUMMARY

C. Kenneth Vogl

Consultant, Towers Perrin

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My testimony addresses two key issues related to pension and OPEB expense.

First, I identify and discuss the primary reasons for increases in FAS 87 pension expense and FAS 106 OPEB expense over the past few years. These reasons are listed below:

- Declining interest rates – Lower interest rates translate into lower discount rates. A lower discount rate increases both the pension and OPEB plan liabilities. The increase in liabilities worsens the funded status of both plans, which increases FAS expense.
- Lower than expected investment returns from 2000-2002 – Trust returns for this period were much lower than the assumed returns for each year. This resulted in fewer assets than expected, which worsened the funded status of the pension and OPEB plans, and ultimately increased FAS expense.
- Higher than expected annual increases in medical costs – Medical inflation has been very high over the past several years (i.e., 10%-20% annual increases). This has caused OPEB plan liabilities to increase, thereby worsening the plan's funded status and increasing expense.

I note the above reasons for increases in pension and OPEB expense were experienced by the majority of other organizations offering these types of plans. AmerenUE's experience has been similar to other companies' experience.

I also describe other changes made by AmerenUE to help offset some of the increase in expenses (e.g., plan amendment to shift some OPEB cost to retirees, reflection of Medicare Part D).

In addition I propose a procedure for the regulatory treatment of pension and OPEB expense. This proposed procedure will ensure that ratepayers are not over- or under-charged for these benefits. This is done by creating a tracking amount (regulatory asset/liability) that continually tracks the mismatch between the actual cost of pension and OPEB benefits and the cost collected in rates for these benefits. This tracking amount is then built into the next rate case. Therefore, over time, the amounts collected in rates will equal AmerenUE's true cost of providing pension and OPEB benefits.

EXECUTIVE SUMMARY

Michael Adams

Director in the Energy Practice
Navigant Consulting, Inc.

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My testimony discusses a lead-lag study for Union Electric Company d/b/a AmerenUE ("AmerenUE" or the "Company") performed by NCI under my supervision, which I used to develop cash working capital factors ("CWC factors"). The CWC factors are used by AmerenUE witness Gary S. Weiss to calculate the cash working capital requirements of the Company.

Cash working capital is the amount of funds required to finance the day-to-day operations of the Company, and should be included as part of AmerenUE's electric business rate base for ratemaking purposes. Cash working capital requirements are generally determined by lead-lag studies that are used to analyze the lag time between the date customers receive service and the date that customers' payments are available to the Company. This lag is offset by a lead time during which the Company receives goods and services, but pays for them at a later date. The results of the lead-lag study and the associated CWC factors are presented in Schedule MJA-G1.

EXECUTIVE SUMMARY

Wilbon L. Cooper

Manager of the Rate Engineering Department
Ameren Services Company

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The purpose of my testimony, and that of my associates, Mr. James R. Pozzo and Mr. William M. Warwick, is to address the following areas of the case:

Sales/Revenues
Class Cost of Service
Rate Design
Miscellaneous Tariff Revisions

<u>Sales/Revenues</u>

Weather normalized sales, revenues and rate billing units, for the twelve month ending June 2006 test year, were developed by Mr. Pozzo and are provided in his Schedules for use in the subsequent design of final rates as a part of this case.

<u>Class Cost of Service</u>

Mr. William Warwick has performed a fully embedded class cost of service study that produced cost of service based revenue requirements at equal class rates of return for the test year ended June 2006. Additionally, Mr. Warwick's study further delineated the study classified the costs as customer related or demand related for the development of specific rates within the classes. The class revenue requirements from this study result in the following base or margin rate percentage increases for the Company's major customer classes: Residential 28%, General Service 16%, Interruptible Service 5%, Standard Transportation Service (-12%), Large Volume Transportation Service (-21%).

It should be reinforced that the above "increase" percentages do not reflect the true impact on a customer's bill. Typically, the base rate or margin component of a gas sales customer represents a third or less of the total bill. The remaining component of the bill is gas supply or PGA which typically represents two-thirds or more of a sales customer's bill. As a result, the percentage increases above should be divided by three for a rough estimate of the total impact on customer bills.

Rate Design

While cost based rates are the starting point in developing class revenue targets and rate design, considering the cost based 28% increase to the residential class and the 12% and 21% reductions to the Standard Transportation ("ST") and Large Volume Transportation ("LVT") classes, respectively, the Company is proposing to maintain existing revenue levels for the ST and LVT classes and to reduce the cost based Residential class' revenue requirement by the equivalent of the cost based reductions to the ST and LVT classes. The Company recognizes the importance of cost based rates, however, other rate principles may be used to guide rate design. These principles include, but are not limited to, rate impact and public acceptability. Residential customers have been hit hard by increases in healthcare costs, housing costs, gasoline, and natural gas commodity prices. Unlike some businesses, residential consumers have little to no opportunity to pass those increases on to others or, in many cases, to afford to invest in conservation or other energy sources. Due consideration to cost of service, rate impact, and public acceptability rate principles provide support for the reasonableness of the Company's proposal. Under the Company's proposal, ST and LVT classes would be no "worse off" than they are today, while residential customers will have their cost based revenue requirement mitigated to some extent. With regard to the General Service and

Interruptible Service rate classes, the Company's proposed rate design tracks the cost of service based revenue requirements. Additionally, currently the Company has two sets of base or margin rates, one for the non-Rolla service areas and one for the Rolla service area. The Company is proposing to merge or combine the above-mentioned base rate structures of the Company's Rolla System to be consistent with the Company's existing base rate structure for the overwhelming majority (approximately 97%) of its natural gas customers.

Miscellaneous Tariff Revisions

The Company is proposing several miscellaneous tariff revisions that are primarily of a housekeeping nature. These tariff language changes have been proposed to improve ease of customer understanding and administration. Additionally, certain changes are being proposed to address service conditions of which there are very limited applications.

EXECUTIVE SUMMARY

John F. Wiedmayer

Project Manager, Depreciation Studies Practice
Gannett Fleming, Inc.

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The purpose of my testimony is to sponsor the depreciation study conducted for Union Electric Company d/b/a AmerenUE, titled "Depreciation Study – Calculated Annual Depreciation Accruals Related to Gas Plant at December 31, 2005." My testimony addresses (1) the methods and procedures I used in the depreciation study, (2) the statistical analyses of service life and salvage data I performed, (3) my estimates of survivor curves and net salvage percents, (4) my calculation of depreciation accrual rates, (5) my proposed amortization of the reserve variance and (6) several examples of the manner in which the study results are presented in the depreciation study report. The specific annual depreciation accrual rates that I recommend the Commission approve are presented in Schedule 1 of Schedule JFW-G1 and the remaining life amortization of the variance between the calculated accrued depreciation and the book accumulated depreciation that I have determined are presented in Schedule 2 of Schedule JFW-G1.

These annual depreciation accrual rates and the reserve variance amortization are based on standard professional and industry practices using estimates of survivor curves and net salvage percents. These estimates are based on informed judgment that incorporates statistical analyses of historical retirement data, field reviews of the property, discussions with management regarding the outlook for plant, and a review of the estimates made for other gas utilities.