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DEC 11 2009

Missouri Public
Service Commission

Exhibit No.:	Michael Gorman
Witness:	Surrebuttal Testimony
Type of Exhibit:	Interim Rates
Issues:	Missouri Industrial Energy Consumers
Sponsoring Party:	ER-2010-0036
Case No.:	

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

_____)
In the Matter of Union Electric Company,)
d/b/a AmerenUE's Tariffs to Increase Its)
Annual Revenues for Electric Service)
 _____)

Case No. ER-2010-0036
Tariff Nos. YE-2010-0054
and YE-2010-0055

Surrebuttal Testimony and Schedule of

Michael Gorman

On behalf of

Missouri Industrial Energy Consumers

November 24, 2009



BRUBAKER & ASSOCIATES, INC.
CHESTERFIELD, MO 63017

MIEC Exhibit No. S
 Case No(s) ER-2010-0036
 Date 12-07-09 Rptr KF

Project 9187

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Union Electric Company,
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STATE OF MISSOURI)

) SS

COUNTY OF ST. LOUIS)

Affidavit of Michael Gorman

Michael Gorman, being first duly sworn, on his oath states:

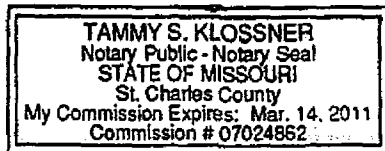
1. My name is Michael Gorman. I am a consultant with Brubaker & Associates, Inc., having its principal place of business at 16690 Swingley Ridge Road, Suite 140, Chesterfield, MO 63017. We have been retained by the Missouri Industrial Energy Consumers in this proceeding on their behalf.

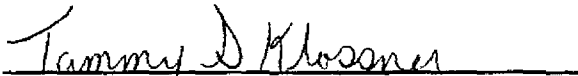
2. Attached hereto and made a part hereof for all purposes are my surrebuttal testimony and schedule which were prepared in written form for introduction into evidence in Missouri Public Service Commission Case No. ER-2010-0036.

3. I hereby swear and affirm that the testimony and schedule are true and correct and that they show the matters and things they purport to show.


Michael Gorman

Subscribed and sworn to before me this 23rd day of November, 2009.




Notary Public

**BEFORE THE PUBLIC SERVICE COMMISSION
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and YE-2010-0055

Surrebuttal Testimony of Michael Gorman

1 Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

2 A Michael Gorman. My business address is 16690 Swingley Ridge Road, Suite 140,
3 Chesterfield, MO 63017.

4 Q ARE YOU THE SAME MICHAEL GORMAN WHO FILED DIRECT AND REBUTTAL
5 TESTIMONY IN THIS PROCEEDING?

6 A Yes, I am.

7 Q WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?

8 A I will respond to certain assertions made in the rebuttal testimony of AmerenUE
9 witnesses Mr. Warner L. Baxter and Mr. Gary S. Weiss.

10 **Response to Mr. Baxter**

11 Q WHAT IS THE FIRST ISSUE MR. BAXTER RAISES IN HIS REBUTTAL
12 TESTIMONY TO WHICH YOU WISH TO RESPOND?

13 A Mr. Baxter asserts that I mischaracterized his testimony concerning regulatory lag.
14 He states that I did not completely articulate his views concerning regulatory lag in his
15 direct testimony.

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1 While he appears to continue to acknowledge that regulatory lag can be good
2 for both customers and for utilities depending on the position in the utility's capital
3 expenditure cycle, he adds that "excessive" regulatory lag creates significant financial
4 challenges for utilities and creates a strong disincentive to make discretionary
5 investments due to the rising cost environment and significant investment cycle in
6 which AmerenUE is currently operating. He further states that his direct testimony
7 was clear that AmerenUE is experiencing excessive regulatory lag in Missouri and
8 concluded that regulatory lag of the magnitude AmerenUE is experiencing in Missouri
9 is excessive and not in the best long-term interest of AmerenUE's shareholders.
10 (Rebuttal testimony, page 3, lines 1-14).

11 **Q DO YOU BELIEVE THAT MR. BAXTER WAS CLEAR THAT IT WAS ONLY**
12 **EXCESSIVE REGULATORY LAG WHICH HE OPPOSED IN HIS DIRECT**
13 **TESTIMONY?**

14 **A No. At page 1, lines 15-20 of his direct testimony, Mr. Baxter states as follows:**

15 The purpose of my direct testimony is to present information which
16 indicates that regulatory lag inherent in Missouri's regulatory
17 framework is systematically preventing AmerenUE from recovering its
18 cost of service and earning its authorized return. In addition, I will
19 provide my perspective on the key drivers and the related policy
20 implications of regulatory lag in Missouri, including the fact that
21 excessive regulatory lag creates significant financial challenges and
22 provides a strong disincentive ... (Emphasis added).

23 I want to be clear, it was not my intention to mischaracterize Mr. Baxter's testimony.
24 However, as apparent in the quote from his direct testimony above, Mr. Baxter was
25 anything but clear that he is only concerned with "excessive" regulatory lag.

26 Mr. Baxter's direct testimony appeared to be clear in that he raises two issues.
27 First, the regulatory framework inherent in Missouri is systematically preventing

1 AmerenUE from recovering its cost of service. Second, Mr. Baxter emphasized his
2 opinion that "excessive" regulatory lag creates a disincentive to invest in utility plant.

3 I do not want to belabor the point, but it was not my intention to misrepresent
4 Mr. Baxter's testimony.

5 **Q HOW DID MR. BAXTER DEFINE "EXCESSIVE" REGULATORY LAG?**

6 **A** Mr. Baxter did not define what he meant by "excessive" regulatory lag.

7 However, in his direct testimony, he did outline certain points which he
8 believed created "significant" regulatory lag in Missouri. Those items at pages 16 and
9 17 of his direct testimony included the following:

- 10 1. Setting rates based on historical costs,
- 11 2. An 11-month suspension period for setting rates, and
- 12 3. Prohibiting utilities from recovering the cost of investment in plant as well
13 as other related financing costs during construction until the plant is fully
14 operational and used and useful.

15 **Q DO YOU BELIEVE THAT THE PARAMETERS IDENTIFIED BY MR. BAXTER AS**
16 **SIGNIFICANT REGULATORY LAG WOULD SUPPORT HIS ASSERTION THAT**
17 **MISSOURI'S REGULATORY PRINCIPLES INCLUDE EXCESSIVE REGULATORY**
18 **LAG?**

19 **A** No. His first point deals with setting rates based on historical costs in Missouri.
20 Mr. Baxter implies that this prevents AmerenUE from setting rates to reflect its cost of
21 service during the period rates will be in effect. However, his assertion contradicts
22 Ameren's practice in Illinois to elect to use historical costs to set rates, despite the
23 fact that the Ameren Illinois utility affiliates have the option to use a "future test year"
24 in Illinois which would set rates based on forecasted costs. In the Ameren Illinois

1 current gas and electric rate cases and since at least the year 2000, the Ameren
2 Illinois Utilities chose to use historical cost test years and historical costs to set rates.
3 To my knowledge, the Ameren Illinois utility affiliates have never elected the future
4 test year or forecasted cost of service option, to set rates. The only departure from
5 the use of historical costs in Illinois is to reflect known and measurable changes.
6 Mr. Baxter's assertion that Missouri's requirement to set rates based on historical
7 costs creates excessive regulatory lag is undermined by Ameren's consistent election
8 to use historical costs to set rates for its Illinois utility affiliates.

9 Mr. Baxter's second point is also not well-founded. Illinois and Missouri both
10 have 11-month suspension periods. As discussed below, AmerenUE's
11 representations to the investing public indicate that Illinois' and Missouri's recent rate
12 decisions have been constructive.

13 Mr. Baxter's third point deals with currently recovering carrying charges and
14 other financial costs associated with construction work in progress (CWIP). While it is
15 true that Missouri utilities are not allowed to recover CWIP carrying costs currently,
16 Missouri utilities are allowed to accrue Allowance for Funds Used During Construction
17 carrying charges and recover those costs after the asset is placed in-service. As
18 such, these costs are not lost forever, but are fully recovered from customers after the
19 asset is used to provide service.

20 To the extent a major construction project is expected to impair a utility's cash
21 flows during construction, there are at least two examples in Missouri (Kansas City
22 Power and Light Company, and The Empire District Electric Company) where a
23 regulatory plan was agreed to by all major stakeholders and approved by the
24 Commission. It allowed for regulatory amortization that enhanced their cash flows
25 during construction and supported their financial integrity and credit rating during

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1 construction. Hence, Missouri regulatory procedures do support utility financial
2 integrity during construction, and also provide full recovery of all reasonable and
3 prudent costs after the asset is placed in-service. Mr. Baxter's assertions concerning
4 CWIP are misplaced.

5 **Q DID MR. BAXTER NOTE WHERE HE BELIEVES AMERENUE IS IN ITS CURRENT**
6 **CONSTRUCTION CYCLE?**

7 A Yes. He asserts that he sees a period in the foreseeable future where AmerenUE's
8 investments in utility plant in-service will not result in a decline in net utility rate base.
9 Because of the outlook for a growing rate base, Mr. Baxter seems to conclude that
10 Missouri's existing regulatory framework and the resulting regulatory lag creates a
11 strong disincentive for AmerenUE to pursue new investments. He asserts that new
12 investment will be necessary to meet increasing customer demands, comply with
13 state and federal regulatory policies, and to support initiatives needed to fuel the
14 state's economy and create jobs.

15 **Q DID MR. BAXTER OUTLINE HIS EXPECTATIONS CONCERNING UTILITY**
16 **PRICING THAT WILL SUPPORT THE STATE'S ECONOMY AND CREATE JOBS?**

17 A Not specifically. Mr. Baxter did comment in his direct testimony that AmerenUE's
18 residential rates are competitive in comparison to national averages, and with other
19 Missouri utilities. However, he has not specifically addressed the need for stable,
20 competitive, and predictable utility pricing in order to support a robust industrial base
21 and related jobs in the AmerenUE service territory.

22 Current Missouri regulatory procedures allow for constructive ratemaking for
23 Missouri utilities, and do minimize rate adjustments which create unnecessary rate

1 volatility in between rate cases. While regulatory lag is an issue that must be
2 recognized and balanced with appropriate regulatory procedures, unnecessary price
3 volatility is not an appropriate solution.

4 **Q HAS AMERENUE'S EXECUTIVE MANAGEMENT RECOGNIZED THAT MISSOURI**
5 **REGULATION PRODUCES CONSTRUCTIVE REGULATORY DECISIONS AND**
6 **RATE ADJUSTMENTS FOR AMERENUE?**

7 A Yes. In a presentation to the Edison Electric Institute Financial Conference in
8 November, 2009, Ameren Corporation's President and CEO Tom Voss made a
9 presentation which included an assessment of the investment highlights of Ameren
10 Corporation and recent rate decisions in Missouri and Illinois. In that presentation,
11 Mr. Voss informed investors that in 2008, AmerenUE received a constructive electric
12 rate case outcome including the implementation of a fuel adjustment clause. Mr.
13 Voss also characterized the rate decisions in Illinois as constructive.

14 Marty Lyons, Ameren Corporation's Senior Vice President and Chief Financial
15 Officer, also noted in that same presentation to the Edison Electric Institute Financial
16 Conference that the pending rate cases in Illinois and in Missouri include an
17 11-month process to receive a final rate determination. Clearly, Ameren Corporation
18 believes that the rate treatment in Missouri and Illinois has been constructive, and
19 both jurisdictions have an 11-month suspension period in order to fully evaluate a
20 utility's cost structure before rates are adjusted.

21 **Q DID MR. BAXTER ASSERT THAT YOU FAILED TO CONSIDER THE LEGITIMATE**
22 **INTERESTS OF THE COMPANY'S SHAREHOLDERS?**

23 A Yes. At page 4 of his testimony, he states the regulatory framework should not

1 prevent a utility from having a reasonable opportunity to earn a fair return, and if it
2 does, then the Commission should take steps to address this issue.

3 **Q DID MR. BAXTER PROVIDE EVIDENCE THAT THE CURRENT REGULATORY**
4 **MECHANISMS IN MISSOURI PREVENT AMERENUE FROM HAVING A**
5 **REASONABLE OPPORTUNITY TO EARN A FAIR RATE OF RETURN?**

6 A No. As outlined in my direct testimony, and as further discussed below in response to
7 Mr. Weiss, the Company has failed to provide evidence that supports its claim that
8 the regulatory mechanisms in use in Missouri today do not provide the Company a
9 reasonable opportunity to earn a fair rate of return.

10 **Q DO YOU HAVE ANY GENERAL COMMENTS ABOUT THE NEED TO CONSIDER**
11 **SHAREHOLDER INTERESTS IN THE DEVELOPMENT OF JUST AND**
12 **REASONABLE UTILITY RATES?**

13 A Yes. Mr. Baxter fails to recognize that businesses that operate in AmerenUE's
14 service territories also have shareholders. The public interest requires that the
15 Commission fairly balance the interest of all stakeholders, including the shareholders
16 of the MIEC and other companies forming Missouri's economic base, when it sets
17 utility rates. While utility shareholders are entitled to a reasonable opportunity to earn
18 a fair rate of return, that opportunity should not be interpreted as a guarantee of
19 earning a fair rate of return. Further, shareholders of AmerenUE's business and
20 industrial customers are entitled to receive utility service at competitive and stable
21 prices. Missouri's regulatory mechanisms should not create undue rate volatility that
22 will erode AmerenUE's management's obligations to manage costs. Competitive
23 utility prices and stable utility rates are essential factors to enable utility customers to

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1 compete in their own markets. Reasonable rates are critical to create Missouri jobs
2 and attract capital investment to Missouri. Shareholders of all stakeholders should be
3 considered in establishing Missouri regulatory mechanisms.

4 **Q DOES THE RECORD SUPPORT AMERENUE'S CONTENTION THAT**
5 **RATE-SETTING IN MISSOURI HAS NOT PROVIDED AMERENUE AN**
6 **OPPORTUNITY TO EARN A FAIR RATE OF RETURN?**

7 A No. While I take issue with the Company's demonstration of actual earned rate of
8 return in relationship to its authorized rate of return over the last two years, the
9 Company did not provide a clear long-term picture of the effectiveness of the
10 regulatory mechanisms in Missouri. Indeed, as outlined in Staff witness Stephen M.
11 Rackers' rebuttal testimony at page 5, when a longer-term perspective is considered
12 (starting in 1996), more in line with a full construction cycle, it shows that AmerenUE's
13 earned rate of return exceeds its authorized rate of return in many periods, and at
14 other points of the construction cycle its earned rate of return is lower than its
15 authorized rate of return.

16 This is precisely the cyclical pattern that is expected to exist.

17 **Response to Mr. Weiss**

18 **Q AT PAGE 3 OF MR. WEISS'S REBUTTAL TESTIMONY, HE DISAGREES WITH**
19 **YOU THAT HIS REVIEW OF ACTUAL EARNED RETURNS ON EQUITY RELATIVE**
20 **TO THE LAST AUTHORIZED RETURNS ON EQUITY DOES NOT SUPPORT THE**
21 **COMPANY'S REQUEST FOR INTERIM RATE RELIEF. DID HE PROVIDE**
22 **EVIDENCE IN SUPPORT OF THIS ASSERTION?**

23 A No. He simply concludes that since AmerenUE's earned returns on equity since June

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1 2007 have consistently fallen short of its authorized returns, the Company is being
2 hurt by excessive regulatory lag and it does not have a reasonable opportunity to
3 earn a fair rate of return.

4 This argument is largely conjecture and unsupported. Indeed, evidence
5 provided by Staff clearly shows that a comparison of actual earned returns on equity
6 in comparison to authorized returns on equity since 1996 reveals that the regulatory
7 process in Missouri has provided AmerenUE an opportunity to earn more than its
8 allowed or ceiling return on equity. The relatively short time period reviewed by Mr.
9 Weiss simply does not support his contention that regulatory lag is something the
10 Company cannot manage, and it certainly does not support the notion that there is
11 somehow "excessive" regulatory lag in Missouri regulatory procedures.

12 **Q DID MR. WEISS DEFINE EXCESSIVE REGULATORY LAG?**

13 A No. The definition and determination of what constitutes "excessive" regulatory lag
14 are completely missing from the Company's presentation.

15 **Q DID MR. WEISS ALSO RESPOND TO YOUR CONTENTION THAT THE**
16 **INCREASE IN THE COMPANY'S REVENUE REQUIREMENT FOR NET PLANT**
17 **GROWTH SINCE THE LAST RATE CASE WILL LARGELY BE OFFSET BY A**
18 **REDUCTION IN ITS COST OF CAPITAL SINCE THE LAST RATE CASE?**

19 A Yes. Mr. Weiss asserts that Ameren Corporation just issued common equity, and
20 part of those proceeds will be used to make equity contributions to AmerenUE. That
21 equity contribution will be reflected at the time of the true-up in this case, and
22 AmerenUE's common equity ratio after the true-up will be higher than it was in the
23 initial filing.

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1 Q DOES THIS ASSERTION ELIMINATE THE REVENUE REQUIREMENT
2 DIFFERENTIAL YOU IDENTIFIED IN YOUR DIRECT TESTIMONY?

3 A No. According to a news release on Ameren Corporation's website,¹ it planned to go
4 to the market for a public offering of new common shares in September 2009. It
5 stated that those shares could be sold over a 30-day period. Hence, equity
6 contributions into AmerenUE from Ameren Corporation likely will not take place until
7 after September 2009. The current rates from AmerenUE's last rate case in Missouri
8 went into effect March 1, 2009. Yet the additional common equity from the sale of
9 common stock will not change AmerenUE's capital structure until end of
10 September/beginning of October 2009. That is approximately a six-month lag from
11 the period rates were originally set in AmerenUE's last rate case and the time
12 AmerenUE's capital structure was adjusted for this new common equity.

13 Hence, for approximately this five- to six-month period, at a minimum,
14 AmerenUE's rates were set to provide a return on a capital structure composed of
15 52% common equity, when its actual capital structure contained only approximately
16 47% common equity. AmerenUE's actual quarterly 2009 capital structure is shown
17 on my Schedule MPG-S-1.

18 Since this interim testimony concerns the effects of leads and lags on rate-
19 setting in Missouri, it is important to recognize that the Company's capital structure
20 has been less expensive than the capital structure it represented to the Commission
21 to set rates for at least a six-month period. Also, when equity is infused in
22 AmerenUE, it is not clear what AmerenUE's actual common equity ratio will be after
23 that equity infusion.

¹"Ameren Corporation Announces Intention to Offer Common Stock," September 8, 2009.

1 Q ARE THERE ANY OTHER ISSUES MR. WEISS RAISED WITH YOUR
2 IDENTIFICATION OF REGULATORY LAG MECHANISMS?

3 A Yes. At page 5 of his rebuttal testimony, Mr. Weiss asserts that the earned return on
4 equity for AmerenUE was improved because of certain deferred accounting
5 mechanisms that are approved for use in Missouri. In effect, Mr. Weiss argues that
6 because of deferral accounting type mechanisms, the Company's return on equity is
7 approximately 100 basis points higher, because \$50 million of operations and
8 maintenance (O&M) expenses were deferred.

9 Q DOES MR. WEISS'S REALIZATION THAT THE COMPANY HAS DEFERRED
10 ACCOUNTING MECHANISMS SUPPORT THE COMPANY'S CONTENTION THAT
11 MISSOURI REGULATORY PROCEDURES CONTAIN EXCESSIVE REGULATORY
12 LAG?

13 A No. Indeed, deferred accounting mechanisms are a means of mitigating regulatory
14 lag because deferral accounting will protect a utility's earnings during a regulatory lag
15 period. Mr. Weiss's assertion that these regulatory mechanisms allowed AmerenUE
16 to defer over \$50 million of O&M expenses, which strengthened its return on equity
17 by over 100 basis points, is clear proof that the regulatory mechanisms in Missouri
18 protect AmerenUE's earnings from the detrimental effects of excessive regulatory lag.

19 Q AT PAGE 1 OF MR. WEISS'S REBUTTAL TESTIMONY, HE STATES THAT
20 MR. RACKERS' REBUTTAL TESTIMONY VERIFIES HIS CALCULATION OF THE
21 REVENUE REQUIREMENT OF NET PLANT ADDITIONS. PLEASE RESPOND.

22 A Mr. Weiss is incorrect that Mr. Rackers agreed with his estimated revenue
23 requirement for net plant additions. Indeed, in Mr. Rackers' rebuttal testimony, he

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1 states that Mr. Weiss overstated the revenue requirement associated with these net
2 plant additions for two reasons. First, Mr. Weiss did not properly account for changes
3 in accumulated deferred income taxes. Second, Mr. Weiss failed to recognize that
4 certain of the plant additions were for new revenue connections. Mr. Rackers then
5 estimated that of the \$37.3 million, approximately \$8.6 million would be overstated.
6 The corrected interim revenue requirement for these new plant additions that do not
7 support investments that will create additional revenue for the utility is \$28.7 million.

8 This revision to the incremental revenue requirement for these new plant
9 additions is significant, particularly when one compares this incremental revenue
10 requirement increase to the revenue requirement savings created because
11 AmerenUE's capital structure has less common equity than the capital structure used
12 by the Commission to set AmerenUE's rates in its last rate case. This incremental
13 revenue requirement increase of \$28.7 million is almost completely offset by the
14 \$24.5 million revenue requirement decrease created by AmerenUE's lower cost
15 capital structure. Hence, the Company's representation that these incremental
16 revenue requirements constitute "excessive" regulatory lag is unfounded.

17 **Q CAN YOU PLEASE SUMMARIZE YOUR POSITION ON AMERENUE'S**
18 **RECOMMENDATION FOR INTERIM RATES IN THIS PROCEEDING?**

19 **A** Yes. I believe AmerenUE's request for interim rate relief should be rejected for the
20 following reasons:

- 21 1. AmerenUE already benefits from regulatory mechanisms which protect it from
22 "excessive" regulatory lag including a fuel adjustment clause, pension/OPEB
23 tracker mechanisms, and accounting deferrals of significant expense.
- 24 2. AmerenUE's earnings over its last construction cycle show that its earnings have
25 been above, and below, its authorized return on equity and therefore regulatory
26 lag has worked both ways. Hence, AmerenUE does have a reasonable
27 opportunity to earn its authorized return on equity. Missouri's regulatory principles

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1 provide strong and effective economic incentive to improve efficiency and to
2 provide fair compensation.

3 3. Regulatory lag in Missouri is no more detrimental to investors than it is to
4 customers, and creates a balanced procedure to set rates that create an incentive
5 for AmerenUE to efficiently manage costs.

6 4. The facts in this case show there is significant cost decreases since AmerenUE's
7 last rate case, that largely offset the cost increases identified by AmerenUE in
8 support of its request for interim rate relief.

9 Hence, a need for an interim rate relief for specific line items is simply not justified.

10 **Q DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

11 **A Yes, it does.**

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AmerenUE

Historical Capital Structures

<u>Line</u>	<u>Description</u>	<u>12/31/2008</u> ¹	<u>3/31/2009</u> ²	<u>6/30/2009</u> ³
1	Long-Term Debt	\$ 3,354,826	\$ 3,703,812	\$ 3,703,972
2	Short-Term Debt	\$ 342,987	\$ 296,739	\$ 460,000
3	Preferred Stock	\$ 113,760	\$ 113,760	\$ 113,760
4	Common Equity	\$ <u>3,447,889</u>	\$ <u>3,392,179</u>	\$ <u>3,427,077</u>
5	Total Capital	\$ 7,259,462	\$ 7,506,490	\$ 7,704,809

With Short-Term Debt

6	Long-Term Debt	46.21%	49.34%	48.07%
7	Short-Term Debt	4.72%	3.95%	5.97%
8	Preferred Stock	1.57%	1.52%	1.48%
9	Common Equity	<u>47.50%</u>	<u>45.19%</u>	<u>44.48%</u>
10	Total Capital	100.00%	100.00%	100.00%

Without Short-Term Debt

11	Long-Term Debt	48.50%	51.37%	51.13%
12	Short-Term Debt	0.00%	0.00%	0.00%
13	Preferred Stock	1.64%	1.58%	1.57%
14	Common Equity	<u>49.85%</u>	<u>47.05%</u>	<u>47.30%</u>
15	Total Capital	100.00%	100.00%	100.00%

Sources:

¹ AmerenUE, FERC Form-1.

² AmerenUE, FERC Form 3-Q.