STATE OF MISSOURI
PUBLIC SERVICE COMMISSION

At a session of the Public Service Commission held at its office in Jefferson City on the 28th day of June, 2007.

In the Matter of Union Electric Company d/b/a AmerenUE's Tariffs Increasing Rates for Electric Service Provided to Customers in the Company's Missouri Service Area	))))	**Case No. ER-2007-0002**

ORDER DENYING APPLICATIONS FOR REHEARING, GRANTING CLARIFICATION, AND CORRECTING ORDER NUNC PRO TUNC

Issue Date: June 28, 2007 Effective Date: July 8, 2007

On May 22, 2007, the Commission issued a Report and Order regarding Union Electric Company d/b/a AmerenUE's tariffs to increase its rates for electric service. That Report and Order became effective on June 1. On May 31, the Office of Administration and the Department of Economic Development (the State of Missouri); the Consumers Council of Missouri; the Missouri Industrial Energy Consumers; the Office of the Public Counsel; and AmerenUE filed timely applications for rehearing. AmerenUE filed a response to the other applications for rehearing on June 11. No other responses were filed.

Section 386.500.1, RSMo (2000), indicates the Commission shall grant an application for rehearing if "in its judgment sufficient reason therefor be made to appear." The applications for rehearing restate the positions the parties espoused at the hearing.

The Commission rejected those positions in its Report and Order. Each application for rehearing will be denied.

The Commission will, however, address an issue raised in the applications for rehearing to further explain the Commission's decision. The applications for rehearing filed by Public Counsel, the State, the Consumers Council of Missouri, and MIEC, note that the Commission's Report and Order spoke approvingly of the testimony offered by MIEC's expert witness, Michael Gorman, regarding an appropriate return on equity. As indicated in the Report and Order, Gorman's overall recommendation for a return on equity was 9.8 percent, but the Commission found a 10.2 percent return on equity to be appropriate. The requests for rehearing seize upon one sentence of the Report and Order that states Gorman's overall recommendation should be "pushed up a bit in recognition of the Commission's denial of AmerenUE's request for a fuel adjustment clause." Based on that sentence, the parties argue that the Commission arbitrarily and inappropriately added .4 percent to the allowed return on equity for the denial of a fuel adjustment clause.

That argument ignores the bulk of the Commission's explanation for why it found a 10.2 percent return on equity to be appropriate. In fact, as indicated in the Report and Order, the Commission found Gorman's Bond Yield Plus Risk Premium Model and Capital Asset Pricing Model, both indicating an appropriate return on equity of 10.2 percent or greater, to be more reasonable than his DCF analysis that resulted in a recommended return on equity of 9.2 percent. Gorman's proxy group for his DCF analysis consisted of 13 comparables, which was smaller and less reliable than the proxy groups suggested by some of the other experts providing return on equity testimony in this case. Thus an

upward adjustment to account for manipulation of the proxy group to achieve an artificially low number is appropriate.

Gorman's testimony, in its totality, was and is the most credible of all the testimony offered on the issue; however, it was not without its shortcomings as evidenced above and with regard to the issue of fuel adjustment. Gorman failed to identify which members of his proxy group were already operating with a fuel adjustment clause and what the effect might be on the company if its request for a fuel adjustment mechanism were denied. There is abundant evidence in this proceeding and in other proceedings before this Commission that most vertically-integrated utilities operating in states that are not restructured have fuel adjustment clauses and less risk. When Billie LaConte, the return on equity witness for the Missouri Energy Group, was asked the following question by a Commissioner: "If we did not give AmerenUE a fuel adjustment clause, then what would your recommendation be in order to try not to hurt this company?", she replied: "I would suggest that the Commission allow a small adjustment on the return on equity to reflect that, …".[1] Accordingly, it is appropriate to compensate companies with additional basis points for assuming that risk and the addition of 40 basis points to Gorman's recommendation is just and reasonable under these circumstances.

More fundamentally, the criticisms of the Commission's return on equity decisions are based on the mistaken assumption that the Commission must accept, without change, a return on equity recommendation suggested by one of the expert witnesses. None of the return on equity experts offering their testimony in this case recommended a return on equity of 10.2 percent, but the Commission is not limited to simply choosing from among the submitted expert recommendations when establishing a return on equity.

[1] Transcript, Page 2945, Lines 13-18.

Establishing a return on equity is part of the Commission's attempt to establish just and reasonable rates. As the Missouri Court of Appeals has indicated, "[under the statutory standard of 'just and reasonable' it is the result reached not the method employed which is controlling. It is not theory but the impact of the rate order which counts."[2] For all the reasons set out in its Report and Order, the Commission has established a return on equity it believes to be just and reasonable. The criticisms of the return on equity allowed by the Commission are without merit and do not justify rehearing.

The State's application for rehearing also raises a matter that can properly be described as a request for clarification rather than a request for rehearing. In criticizing the Commission's decision to establish an annual base level of SO_2 sales of $5 million, the State points out that while the Commission's decision creates a tracking mechanism to account for sales over and under that $5 million base level, it does not indicate whether AmerenUE should pay interest to ratepayers for accrued sales over that amount, or collect carrying costs from ratepayers if sales fall below the base level. The Commission's Report and Order is silent on that question and that silence could result in confusion and misunderstandings in a future rate case. Therefore, the Commission will clarify its Report and Order to provide that AmerenUE shall pay interest to ratepayers at its short-term borrowing rate for annual accrued SO_2 sales above a base level of $5 million and collect carrying costs from ratepayers at the same rate if sales fall below that base level. Interest or carrying costs shall be calculated based on the amount by which the balance in the tracking account varies from the $5 million baseline established in the Report and Order, on

[2] *State ex rel. Assoc. Natural Gas Co. v. Pub. Serv. Com'n of Missouri*, 706 S.W. 2d 870, 873 (Mo App. W.D. 1985)

December 31, 2007, and each subsequent December 31, until the Commission issues a final order in AmerenUE's next rate case.

AmerenUE's application also raises a matter for which it seeks clarification. At page 95 of its Report and Order, the Commission addresses an issue defined as "Net Salvage Percentage to be Used for Assets in Account 322." In its decision on this issue, the Commission held that an additional .2 percent should be added to the depreciation rate for Account 322. However, the Commission also found that Staff and AmerenUE's agreement that an additional .1 percent should be added to the depreciation rates for other nuclear plant accounts was not identified as a separate issue and was not supported by any evidence. Therefore, the Commission found that it had no basis for making a decision regarding those accounts.

AmerenUE interpreted the Commission's inability to decide whether an additional .1 percent should be added to the depreciation rates for other nuclear accounts to mean that the net salvage percentages for those accounts must be set at zero. As a result, AmerenUE calculated its rates using zero net salvage percentages for those accounts – specifically accounts 321, 323, 324, and 325. Because net salvage percentages for those accounts were set at zero, AmerenUE's allowed revenue requirement was reduced by approximately $1 million below the revenue requirement contemplated in the Report and Order. The compliance tariffs submitted by AmerenUE and approved by the Commission reflect that lower revenue requirement, although AmerenUE indicates it does not believe the Commission intended that result.

AmerenUE explains that the depreciation rates proposed by Staff in its testimony include net salvage percentages of -3 percent for account 321, -3 percent for account 323,

-2 percent for account 324, and -1 percent for account 325. Those net salvage percentages were not challenged by any party and AmerenUE contends the Commission should have ordered it to use those net salvage percentages for those accounts.

AmerenUE is correct. In holding that it lacked sufficient evidence to decide whether to add .1 percent to the net salvage percentages proposed by Staff for accounts 321, 323, 324, and 325, the Commission did not set those net salvage percentages at zero. The net salvage percentages proposed for those accounts by Staff are reasonable and are not opposed by any party. AmerenUE shall use those net salvage percentages when calculating its allowed revenue requirement. AmerenUE may file tariffs to reflect the revised calculations.

AmerenUE also identified three factual errors in the Report and Order that it suggests be corrected nunc pro tunc. First, AmerenUE's legal counsel is identified in the Report and Order as James B. Lowrey. The attorney's last name is in fact spelled Lowery. Second, the Report and Order, at page 9, states that AmerenUE serves approximately 2 million customers in Missouri. In fact, AmerenUE serves approximately 1.2 million Missouri customers. Third, at page 75 of the Report and Order, the Commission indicates it will establish a regulatory tracking mechanism "without including a base amount of SO_2 sales in AmerenUE's revenue requirement." In fact, later in the Report and Order, the Commission included a base amount of $5 million in the regulatory tracker. All the identified factual errors will be corrected nunc pro tunc.

IT IS ORDERED THAT:

1. The Office of Administration and the Department of Economic Development's (the State of Missouri's) Application for Rehearing is denied.

2. The Consumers Council of Missouri's Application for Rehearing is denied.

3. The Missouri Industrial Energy Consumers' Application for Rehearing is denied.

4. The Office of the Public Counsel's Application for Rehearing is denied.

5. Union Electric Company d/b/a AmerenUE's Application for Rehearing is denied.

6. The Commission's Report and Order is clarified to provide that AmerenUE shall pay interest to ratepayers at its short-term borrowing rate for annual accrued SO_2 sales above a base level of $5 million and collect carrying costs from ratepayers at the same rate if sales fall below that base level. Interest or carrying costs shall be calculated based on the amount by which the balance in the tracking account varies from the $5 million baseline established in the Report and Order, on December 31, 2007, and each subsequent December 31, until the Commission issues a final order in AmerenUE's next rate case.

7. The Commission's Report and Order is clarified to provide that AmerenUE shall use the following net salvage percentages when calculating its allowed revenue requirement:

Account 321	-3%
Account 323	-3%
Account 324	-2%
Account 325	-1%

AmerenUE shall file tariffs to reflect the revised calculations.

8. The following items in the Commission's May 22, 2007 Report and Order are corrected nunc pro tunc:

a. In the Appearances section of page 1, the name of AmerenUE's attorney is correctly spelled Lowery, not Lowrey;

b. On page 9, AmerenUE serves approximately 1.2 million Missouri customers, not 2 million; and

c. On pages 74-75 the following sentence is deleted: "For those reasons, the Commission finds it in the long-term best interest of ratepayers to establish a regulatory tracking mechanism without including a base amount of SO_2 sales in AmerenUE's revenue requirement."

9. This order shall become effective on July 8, 2007.

BY THE COMMISSION

Colleen M. Dale
Secretary

(S E A L)

Davis, Chm., Murray, Clayton and Appling, CC., concur
Gaw, C., dissents

Woodruff, Deputy Chief Regulatory Law Judge