MEMORANDUM

TO: Missouri Public Service Commission Official Case File,
Case No. GR-2006-0087, Union Electric Company d/b/a AmerenUE

FROM: David M. Sommerer, Manager - Procurement Analysis Department
Anne Allee, Regulatory Auditor - Procurement Analysis Department
Kwang Choe, Ph.D., Regulatory Economist – Procurement Analysis Department

/s/ David M. Sommerer 12/27/06 — Project Coordinator / Date

/s/ Robert V. Franson 12/27/06 — General Counsel's Office / Date

SUBJECT: Staff Recommendation in Case No. GR-2006-0087, Union Electric Company d/b/a AmerenUE's 2004-2005 Actual Cost Adjustment Filing

DATE: December 27, 2006

The Procurement Analysis Department (Staff) has reviewed Union Electric Company d/b/a AmerenUE's (Company or AmerenUE) 2004-2005 Actual Cost Adjustment (ACA) filing. This filing was made on October 14, 2005, and is docketed as Case No. GR-2006-0087. The filing contains the Company's calculations of the ACA balance.

AmerenUE separates its Missouri gas operations into the following pipeline service areas: Panhandle Eastern Pipe Line (PEPL or Panhandle), Texas Eastern Transmission Corporation (TETCO), and Natural Gas Pipeline Company of America (NGPL). PEPL serves approximately 95,600 customers in the Jefferson City/Columbia area. TETCO serves approximately 19,200 customers in the Cape Girardeau area. NGPL serves approximately 2,000 customers in the Marble Hill area. AmerenUE acquired the Rolla system, formerly the Aquila MPS – Eastern system, on May 1, 2004. PEPL, Missouri Pipeline Company (MPC), and Missouri Gas Company (MGC) serve approximately 3,900 customers in the Rolla, Salem, and Owensville area.

Staff's review included an analysis of the billed revenues and actual gas costs used in the Company's computation of its ACA rates. A comparison of billed revenue recovery with actual gas costs will result in an over-recovery or under-recovery of the ACA balance. Staff also reviewed AmerenUE's gas purchasing practices to determine the prudence of the Company's purchasing decisions.

Because of internal resource limitations, the Staff conducted no reliability review for this ACA period. The Staff's review of the Company 2004-2005 capacity shows that, other than the reduction of capacity to the TETO service area, the contracted pipeline capacity for this period did not change from the previous ACA period.

GAS COST AND REVENUES - CORRECTIONS

The Staff found errors in the Company's recording of gas costs within the ACA filing. These errors resulted in an overstatement of gas costs by $26,932 for the PEPL service area and an understatement of gas costs by $1,145 for the NGPL service area.

Additionally, the Staff found an error related to the recording of revenues in the ACA filing. The Company recorded revenues in the NGPL service area instead of the TETCO service area. This resulted in an overstatement of revenues for the NPGL service area and an understatement of revenues for the TETCO service area of $3,576.

In order to correct both the gas cost and revenue errors, the Staff proposes the following adjustments to the ending ACA balances: decrease PEPL ACA balance by $26,932, decrease the TETCO ACA balance by $3,576 and decrease the NGPL ACA balance by $4,736.

HEDGING

In its gas procurement strategy, AmerenUE engages in long-term planning and procurement for its utility gas supply portfolio to insure system reliability and to mitigate price volatility for its purchased gas adjustment (PGA) sales customers. In particular, the Company's hedging strategy is to hedge against market price volatility. The current supply planning horizon for gas supply purchases and price hedging is thirteen seasons or six and one half years. Gas supply transactions and price hedges for each of the forward thirteen seasons are phased in based upon the proximity to the current season, the current futures prices, the availability of supply and general market conditions. The objective is to create a forward gas supply portfolio and to dollar-cost-average gas supply prices that mitigate price volatility for the PGA sales customers, reduces natural gas supply acquisition risk, enhances system reliability while maintaining flexibility to manage load variations, and separates physical delivery and financial exposure. The primary goal of the hedging strategy is to dampen price swings, not specifically to reduce gas costs to the utility's customers. Beating the market is not considered the object of a successful hedging strategy. The supply portfolio will also seek to diversify credit risk among counterparties which includes purchasing financial price hedging instruments from financial counterparties who are not involved with the physical delivery of natural gas.

Approximately 75% of normal winter requirements will be hedged against market price volatility. Storage withdrawals constitute about 50% of the hedge, and 25% are price hedged by purchasing an embedded price hedge along with the physical gas supply or by purchasing a separate financial contract. Embedded hedges include physical supplies purchased using a NYMEX price structure that can be fixed, physical supplies purchased with a costless price collar, and physical supplies purchased with price caps. Financial contracts include over-the-counter financial swaps and NYMEX futures contracts.

The goal of a hedging plan is to mitigate the price volatility of the commodity (natural gas) for the winter heating season of November through March. AmerenUE's hedging implementation plan was designed to protect approximately 75% of normal winter demand requirements against market price volatility. Three AmerenUE systems, PEPL-UE, TETCO-UE and NGPL-UE, combined were 81% hedged for November 2004 through March 2005 based on actual delivered gas. The price protection, including storage, comes from fixed-forward contracts, and financial natural gas swaps. Hedges utilizing the fixed price contracts and the financial natural gas swaps were placed in late October 2003 and also between late March and early December 2004 for the winter heating season of November 2004 through March 2005. AmerenUE receives regular natural-gas market analyses from energy and financial firms such as Conoco Phillips, Bank of America, UBS Warburg, Deustche Bank, Barclay Capital, BMO Nesbitt Burns, Coral Energy(Shell Trading), J.P. Morgan Chase, Merrill Lynch, Pira at no cost. AmerenUE also uses Risk Management Inc., a paid consultant, for regular market reports and assessments. Although the Company's hedging practice was appropriate for November 2004 through March 2005, the Staff recommends that the Company continue to assess and document the effectiveness of its hedges for the 2005-2006 ACA and beyond.

RECOMMENDATIONS

The Staff recommends the Commission issue an order requiring AmerenUE to:

1. Establish the following account balances in its next ACA filing to reflect the (over)/under recovery of the ACA balances to be (refunded)/collected from the ratepayers as of August 31, 2005:

	Balance per AmerenUE Filing	Staff Adjustments	Ending Balances
Natural Gas Pipeline Co. of America: Firm Sales ACA	$(24,037)	$4,736	$(19,301)
Interruptible Sales	0	0	0
Panhandle Eastern Pipe Line Co: Firm Sales ACA	$3,525,955	$(26,707)	$3,499,248
Interruptible Sales ACA	$152,456	$(225)	$152,231
Former Aquila Eastern System Incremental: Firm Sales	$41,780	0	$41,780
Texas Eastern Transmission Corp: Firm Sales	$425,351	0	$425,351
Interruptible Sales	$234,453	$(3,576)	$230,877

2. Continue to assess and document the effectiveness of its hedges for the 2005/2006 period and beyond.
3. Respond to the recommendations herein within 30 days.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Union Electric Company, d/b/a AmerenUE's Purchased Gas Adjustment Factors to be Reviewed in Its 2004-2005 Actual Cost Adjustment.	))))	Case No. GR-2006-0087

AFFIDAVIT OF DAVID M. SOMMERER

STATE OF MISSOURI)
) ss.
COUNTY OF COLE)

David M. Sommerer, being of lawful age, on his oath states: that as Manager of the Procurement Analysis Department of the Utility Services Division he has participated in the preparation of the foregoing report, consisting of 3 pages to be presented in the above case, that he has verified that the following Staff Memorandum was prepared by Staff of the Procurement Analysis Department that have knowledge of the matters set forth as described below; that he has verified with each of the Staff members listed below that the matters set forth in the Staff Memorandum are true and correct to the best of his/her knowledge and belief,

Anne Allee	Gas Cost and Revenues - Corrections
Kwang Choe:	Hedging

that he has knowledge of the matters set forth in such report and that such matters are true to the best of his knowledge and belief.

David M. Sommerer
David M. Sommerer

Subscribed and sworn to before me this 27th day of December 2006.

D. SUZIE MANKIN
Notary Public - Notary Seal
State of Missouri
County of Cole
My Commission Exp. 07/01/2008

D Suzie Mankin
Notary Public