BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the matter of the application of Union Electric Company for an order authorizing: (1) certain merger transactions involving Union Electric Company; (2) the transfer of certain assets, real estate, leased property, easements and contractual agreements to Central Illinois Public Service Company; and (3) in connection therewith, certain other related transactions.	))))))))	Case No. EM-96-149

MEMORANDUM ON JURISDICTIONAL ISSUES

INTRODUCTION

The Office of the Public Counsel ("Public Counsel") is filing this memorandum because there are jurisdictional issues involved in the Union Electric Company ("UE") and Central Illinois Public Service Company ("CIPS"; together "Applicants") proposal. These issues are too central to the case and too important to be left for post-hearing briefs, and too involved in the law to be addressed by a non-lawyer in testimony. The Missouri Public Service Commission should be aware of the jurisdictional implications of the merger proposal so that they will be prepared to ask questions about jurisdictional issues at the hearing, or even submit written questions to the parties, as was done by the Illinois Commerce Commission in the UE/CIPS merger case in Illinois. Public Counsel does not believe that any party will be prejudiced by

this filing, even though it is not set out in the procedural schedule. Public Counsel encourages the other parties to respond, and requests that the Commission allow them ample time to do so.

THE PUBLIC UTILITY HOLDING COMPANY ACT AND THE SECURITIES AND EXCHANGE COMMISSION

15 United States Code Section 79, the Public Utility Holding Company Act (PUHCA), defines a holding company as:

> any company which directly or indirectly owns, controls, or holds with power to vote, 10 per centum or more of the outstanding voting securities of a public-utility company or of a company which is a holding company by virtue of this clause or clause (B) of this paragraph, unless the Commission, as hereinafter provided, by order declares such company not to be a holding company.... (Section 79b(a)(1)(7)(A); all statutory references herein will be to Chapter 15 of the United States Code, unless otherwise noted).

UE and CIPS propose to merge and create a holding company known as Ameren Corporation. Both UE and CIPS will be wholly-owned subsidiaries of Ameren. (Although both UE and CIPS are currently holding companies, they are both exempt under Section 79c.) Ameren will not seek to be exempt, but rather will be subject to all of the regulatory requirements of PUHCA; it will be what is known as a registered holding company under Section 79e (Application, pages 2-3).

Public Counsel's discovery has not completely resolved the question of why this holding company structure is proposed by Applicants, but it appears to be have been insisted upon by CIPS from the outset. Regardless of where the proposal originated, the consequent loss of the Missouri Commission's jurisdiction is fairly clear. (However, see UE response to Staff DR 143, discussed below.) The consequences of this holding company structure is to vest jurisdiction over many of the transactions between Ameren subsidiaries in the SEC, rather than in the Missouri Commission. The case of Ohio Power Co. v. FERC, 954 F.2d 779 (D.C. Cir. 1992), cert. denied sub. nom, Arcadia, Ohio v. Ohio Power Co., 121 L.Ed.2d 388 (U.S. No. 92-264 and No. 92-280, November 9,1992) is frequently considered to be the case that establishes the SEC's "turf" with respect to holding company subsidiary transactions. In Ohio Power the Court of Appeals for the D.C. circuit held that the FERC could not deny recovery by a utility of coal costs it incurred pursuant to a coal purchase from an affiliate, if that purchase had been approved by the SEC. To do so would improperly trap costs for the utility. (Id., at 971). While that case dealt with the SEC's actions preempting later, inconsistent actions by the FERC, it is widely believed that such preemption may extend to inconsistent state commission action as well. In fact, in response to Staff DR No. 144, UE apparently agreed that one could make preemption arguments based on Ohio Power. However, UE goes on to state in that response:

> While neither agreeing nor disagreeing with the MPSC's "interpretation of Ohio Power", as discussed on page 10 of [the Commission's Notice of Intervention in Docket No. EC96-7-000 before the FERC], UE does not intend to claim that the MoPSC is precluded from questioning the "cost or revenue levels incurred or realized by" UE as a result of the SEC-jurisdictional agreements. (UE Response to Staff DR. No 144).

In response to another Staff DR (No. 143), UE states that:

> Ameren's status as a registered holding company will not affect the authority of the MoPSC over (a) the reasonableness of the terms of any agreements between UE and Ameren or an Ameren affiliate; and (b) the prudence of the decision to enter into such agreements. (Id.)

Taken together, one can infer that UE may believe that it could make a legal argument the SEC rulings preempt state jurisdiction, but that it does not intend to raise such an argument. If this inference is correct, it leads quite well to an approach to federal preemption taken in the CINergy merger cases, discussed below.

THE FEDERAL POWER ACT AND THE FEDERAL ENERGY REGULATORY COMMISSION

The Federal Power Act, ("FPA", 16 U.S.C. Section 791 et seq.) created the Federal Power Commission, now the FERC. Under the FPA, the FERC has jurisdiction over the transmission and sale of electricity in interstate commerce. It also provides for FERC approval of the disposition of interstate transmission facilities. (16 U.S.C. Section 824b and 824c). Since the FERC has exclusive jurisdiction over wholesale and transmission rates, once the FERC has approved these rates a state may not determine that the FERC approved rates are unreasonable.

One of the questions asked by Illinois Commerce Commissioner Kretschmer and the Applicants' response is particularly revealing on the issue FERC/state jurisdiction. The question and answer are quoted at length because of their importance:

> [Question:] Assuming that Ameren is not an exempt holding company under PUHCA, the record should show what authority the ICC will have over: (a) the reasonableness of the rates and terms contained in the System Support and Join Dispatch agreements; and (b) the prudence of the decision to enter such agreements, as they effect CIPS's base rates....

Response: Ameren's status under PUHCA (whether regulated or exempt) does not affect the ICC's authority regarding the System Support and Joint Dispatch Agreements. Irrespective of whether Ameren is a registered holding company, those Agreements will be subject to the jurisdiction of the Federal Energy Regulatory Commission ("FERC"), as would any agreement among utilities, whether they are affiliated or not. Accordingly, the Illinois Commerce Commission will have no authority over the rates, terms or conditions in those agreements. See Mississippi Power & Light Co. v. Mississippi ex. rel Moore, 108 S.Ct. 2428 (1988). Further, the ICC will have no authority to deny recovery from retail ratepayers of charges incurred by CIPS under the FERC-approved agreements.

Applicants have not questioned the Commission's jurisdiction to review the decisions of Union Electric and CIPS to enter into those agreements as matters incident to the Merger. Accordingly, in their Application, Applicants specifically requested that the Commission find that their decisions to enter into those agreements are prudent and reasonable and that the Commission consent thereto. See Application, p. 24.

Applicants would also note that PUHCA generally requires that subsidiaries of holding companies subject to PUHCA, which are capable of integrated operation, operate on an integrated basis (including joint dispatch), if there are savings to be realized by such operation. With regard to the joint dispatch agreement, therefore, the jurisdiction of this Commission reaches only the issue of the prudence of the agreement within the context, and as an element, of the merger. Once the merger is approved, the agreement will be one required by federal law and this Commission will, therefore, not have further prudence jurisdiction. See, e.g., Mississippi Power & Light, supra. Moreover, as noted above, since the agreement is a wholesale transaction between CIPS and Union Electric, jurisdiction over the agreement, its rates, terms and conditions lies with the FERC and not with this Commission. Id.

While the System Support Agreement is not mandated by federal law, it is a basic requirement for transferring the Union Electric Illinois service territory to CIPS. The System Support Agreement enable CIPS to provide service to the former Union

> Electric customers and preserve for those customers the same low cost structure and rates which they have enjoyed as Union Electric customers. Without this agreement, the Applicants would have to reevaluate the transfer of the Union Electric Illinois service territory. Consequently, this Commission must evaluate the prudence of the System Support Agreement in the context of whether the public will be convenienced by the transfer of the Union Electric Illinois service territory to CIPS and in the context of the merger as a whole. Once the service territory is transferred, the Commission not revisit the prudence of entering into such an agreement. See, e.g., Mississippi Power & Light, supra. (UE Response to Staff DR 138).

In other words, speak now or forever hold your peace. Once the two state Commissions approve the various agreements, much of the regulation will pass to federal agencies. The Missouri Commission should be wary of that outcome, and as a result should not approve the merger as proposed. It should at least require UE to agree not to assert federal preemption (this concept is discussed in more detail below), or deny the merger application as detrimental to the public interest.

Applicants refer frequently to Mississippi Power & Light in the above quote. Before discussing that case, some discussion of its "predecessor," Nantahala Power and Light Co. v. Thornburg, 476 U.S. 953 (1986), is warranted. In Nantahala, Nantahala and a sister company, both of which were owned by Alcoa, owned hydroelectric plants. In exchange for the power from these plants, the Tennessee Valley Authority (TVA) provided each company cheap entitlement power in a fixed ratio. The FERC found that the ratio was unfair, and ordered Nantahala to receive a greater percentage and adjust its rates accordingly. Subsequently, The North Carolina Utility Commission (NCUC) set retail rates based on the presumption that Nantahala had more of the cheap entitlement power. The United States

Supreme Court held that the FERC's determination of wholesale rates preempted the NCUC's ability to use a different wholesale rate in setting retail rates.

In Mississippi Power & Light, the FERC ordered MP&L to purchase capacity from the Grand Gulf nuclear power plant, and MP&L sought recovery of those costs in rates. The Mississippi Public Service Commission allowed recovery, but the Mississippi Supreme Court held that the Mississippi Public Service Commission could question that purchase. The United States Supreme Court overturned. The US Supreme Court ruling was grounded on the principle of preemption, which, simply stated, is that the states are not free to second-guess the decisions of federal agencies acting within their authority. The Court stated:

> [A] state utility commission setting retail prices must allow, as reasonable operating expenses, costs incurred as a result of paying a FERC-determined wholesale price...[and] give effect to Congress' desire to give FERC plenary authority over interstate wholesale rates, and to ensure that states do not interfere with this authority. Id., at 371-372.

Note that an apparent exception to the reasoning in these two cases exists in the case of Pike County Light & Power v. Pennsylvania Public Utility Commission, 465 A.2d 735 (Pennsylvania Commonwealth Court 1983). In that case, the Court found that even though the state utility commission could not challenge a rate set by the FERC, it could find a utility imprudent in entering into a contract to pay that rate.

THE " CONTRACT EXCEPTION" TO FEDERAL PREEMPTION

In the proceedings involving the CINergy merger in both Indiana and Ohio, the parties fashioned an agreement designed to resolve concerns over loss of state jurisdiction to the SEC. While such an agreement is not perfect (since its enforcement could be problematic), it has the possibility of ameliorating the harm inherent in the Commission's loss of jurisdiction. With the exception of references to specific parties and regulators, the language used in Indiana and Ohio is virtually identical:

> [A]ll contracts, agreements, or arrangements of any kind, required to be filed with and/or approved by the SEC pursuant to the Public Utility Act of 1935 ... shall contain and be conditioned upon the following without modification or alteration:
>
> The Cincinnati Gas & Electric Company and CINergy will not seek to overturn, reverse, set aside, change or enjoin, whether through appeal or the initiation of any action in any forum, a decision or order of the Public Utilities Commission of Ohio which pertains to recovery, disallowance, allowance, deferral, or ratemaking treatment of any expense, charge, cost, or allocation incurred or accrued by The Cincinnati Gas & Electric Company in or as a result of a contract, agreement, arrangement, or transaction with any affiliate, associate, holding, mutual service or subsidiary company on the basis that such expense, charge, cost or allocation has itself been filed with or approved by the Securities and Exchange Commission, or was incurred pursuant to a contract, arrangement, or allocation method which was filed with or approved by the Securities and Exchange Commission.
>
> Failure to include the above language in any such contract, agreement, or arrangement shall render the same voidable at the sole discretion of the Public Utilities Commission of Ohio. Should the above language be altered or invalidated by any Court or governmental agency, such contract, agreement, or arrangements shall be voidable at the sole discretion of the Public Utilities Commission of Ohio. The foregoing provisions of this Paragraph are contained in the tariff attached hereto as Exhibit 3, which should be approved by the Commission. (In the matter of the Application of the Cincinnati Gas & Electric Company for an Increase in Electric Rates in its Service Area, Case No. 91-410-EL-AIR (On Remand), pages 14-16).

Although this language applies only to preemption by the SEC, a similar approach (using generally similar language) could be taken with respect FERC preemption. Given UE's responses to DRs (discussed above), it appears likely that UE will not object to entering into such "anti-preemption" agreements.

Another related critical issue is access to the books and records of utilities, holding companies, and subsidiaries. In addition to Ohio and Indiana, Arkansas and other states have addressed this question. Language from the Ohio Stipulation cited above is illustrative of how access can be ensured:

> In any pending proceeding before the PUCO, CG&E and its prospective holding company, CINergy Corp (CINergy), agree to make available to the PUCO and the OCC, at reasonable times and places, all books and records and employees and officers of CINergy, CG&E, and any Affiliate or Subsidiary of CINergy or CG&E, as determined relevant by the PUCO under ORC Section 4903.082 and the administrative rules of the PUCO; provided, however, CG&E and CINergy have the right to seek a protective order.... (Id., at 12).

Of course, another solution would be simply for this Commission to reject the merger as currently structured and indicate to the Applicants that it would look more favorably upon a merger that resulted in a unitary structure. Such a structure would create one utility that would serve the former customers of both UE and CIPS. It could retain the names, employees, headquarters, and other aspects of UE and CIPS. Note that this approach is the one that Utilicorp United, Inc. has largely followed.

CONCLUSION

The loss of Missouri Public Service Commission jurisdiction, and the attendant loss of the protection afforded ratepayers by the Commission's oversight, is a real and significant detriment to the public. Unless UE voluntarily makes a binding and enforceable commitment on behalf of Ameren and all subsidiaries to be bound by state commission action and to not argue federal preemption by either the FERC or the SEC, or unless Applicants agree to restructure the merger proposal to eliminate this problem, the merger should not be approved. In addition, unless UE commits to make the books and employees of the holding company and all its subsidiaries reasonably available, the merger should not be approved.

Respectfully submitted,

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