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UNION ELECTRIC

June 6, 1996

VIA FEDERAL EXPRESS

Mr. David L. Rauch
Executive Secretary
Missouri Public Service Commission
P.O. Box 360
Jefferson City, MO 65102

Re: MPSC Docket No. EM-96-149
UE/CIPSCO Merger

Dear Mr. Rauch:

Enclosed for filing on behalf of Union Electric Company in the above matter is an original and fourteen (14) copies of its Legal Memorandum in Response to Staff and Office of Public Counsel.

Kindly acknowledge receipt of this filing by stamping as filed a copy of this letter and returning it to the undersigned in the enclosed envelope.

Sincerely,

William J. Niehoff
Attorney

WJN/bb
Enclosure(s)
cc: Counsel of Record

FILED
JUN 7 - 1996
MISSOURI
PUBLIC SERVICE COMMISSION

#5051

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Docket No. EM-96-149
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CERTIFICATE OF SERVICE

This is to certify that on this 6th day of June, 1996, a copy of the foregoing was mailed via U.S. mail to the parties of record in this proceeding.

William J. Niehoff

#5051

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.	)	Docket No. EM-96-149

LEGAL MEMORANDUM IN RESPONSE TO
STAFF AND OFFICE OF PUBLIC COUNSEL

I.
INTRODUCTION

The Staff of the Missouri Public Service Commission ("Staff") and Office of the Public Counsel ("OPC") filed legal memoranda discussing certain regulatory authority issues with the Missouri Public Service Commission ("MPSC"). Union Electric Company ("UE" or "Company") submits this memorandum to describe the appropriate standard to be used by the Commission in determining whether to approve the merger; to discuss the current status of law regarding the jurisdiction of the Federal Energy Regulatory Commission ("FERC") and the Securities and Exchange Commission ("SEC"); and to express Union Electric's position that it is not opposed to continued Missouri regulation where that authority presently exists. Union Electric has also presented a brief response to the allegation that UE is barred from recovering 1995 transaction costs by the prohibition against retroactive ratemaking.

This memorandum responds to several of the legal issues identified in the testimony and comments of Staff and OPC but is

not intended to be a complete statement of Union Electric's legal position. UE reserves the right to address other legal issues and to submit additional memoranda in the continued course of this proceeding as deemed necessary or appropriate.

II.
THE STANDARD FOR APPROVAL OF THE MERGER DOES NOT REQUIRE EXPANDING STATE REGULATORY AUTHORITY OR PREVENTING ANY DISPLACEMENT OF THAT AUTHORITY BY A FEDERAL AGENCY

A. Union Electric did not choose to organize as a registered holding company in order to avoid Missouri Commission authority.

Union Electric did not choose to proceed under the Public Utility Holding Company Act of 1935, 15 U.S.C. §79 et seq. ("PUHCA"), in order to escape Missouri Commission regulation. If this were its purpose, UE believes that it could have reorganized to come within PUHCA even without the merger with CIPSCO. In fact, in the early 1950's, UE was a registered non-exempt public holding company subject to PUHCA. Nonetheless, as shown below, the potential displacement of some Missouri Commission regulatory authority over Union Electric or Ameren provides insufficient reason to delay approval of the merger.

B. The Commission must approve the proposed merger unless it is shown to be detrimental to the public interest.

Staff, in its legal memorandum, described the standard to be used by the Commission in determining to approve this merger as follows:

> Under Missouri law the Commission must approve the proposed merger unless it is detrimental to the public interest.

Comments of Staff Counsel ("Comments"), p. 2, (emphasis supplied); see also, Rebuttal Testimony of Cary G. Featherstone, pp. 13-14. The language cited by Staff comes directly from an opinion by the Missouri Supreme Court in which it was held that public utilities have the right to transfer or dispose of property absent demonstrable harm to the public interest:

> The owners of this stock should have something to say as to whether they can sell it or not. To deny them that right would be to deny them an incident important to ownership of property. *City of Ottawa v. Public Service Commission*, 130 Kan 867, 288 P. 556. A property owner should be allowed to sell his property unless it would be detrimental to the public.

State ex rel. City of St. Louis v. Public Service Commission of Missouri, 73 S.W.2d 393 (Mo. 1934). More recently, the court used this standard in State ex rel. Fee Fee Trunk Sewer, Inc. v. Litz, 596 S.W.2d 466 (Mo.App. 1980), wherein it stated:

> The obvious purpose of this provision [§393.190 RSMo. (1969)] is to ensure the continuation of adequate service to the public served by the utility. The Commission may not withhold its approval of the disposition of assets unless it can be shown that such disposition is detrimental to the public interest. (Citation omitted).

Id., 596 S.W.2d at 468 (emphasis supplied). Thus, the appropriate standard to be used in determining whether to approve the merger is not whether some Missouri Commission regulatory authority is preempted by the SEC or the FERC, but whether the proposed merger is detrimental to the continuation of adequate service to the public served by the utility.

There does not appear to be any precedent in Missouri permitting denial of a merger on the basis that some Missouri

Commission authority is or will thereby be preempted. In its brief, Staff argued, without citation to authority, that:

> One of the factors the Commission may consider in determining if this standard is met is whether effective MoPSC regulation will be impaired or diminished by the merger.

Comments, at 2 (emphasis supplied). Likewise, without citation to authority, OPC appears to have assumed continued Missouri Commission regulation must be maintained as a condition for merger approval.[1]

If the limited preemption of Missouri Commission authority by the FERC or the SEC were sufficient cause for the Missouri Commission to withhold approval of the merger, it would be logical for Commission regulations regarding mergers to state this fact. e.g. Commonwealth Edison Co., 36 FPC 927 (1966), aff'd sub nom. Utility Users League v. FPC, 384 F.2d 16 (1966), cert denied, 393 U.S. 953 (1968). In fact, appropriate regulations do not contain any requirement that the effect of the merger on state regulation be considered. 4 CSR § 240-2.060 (6)(A)-(H). Instead, consistent with the opinions cited above, the regulations require only that merger applications contain a statement of the reasons that the proposed merger is "not detrimental to the public interest". 4 CSR §240-2.060 (6)(D).

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[1] Neither Staff nor OPC argue that, because of the merger, Union Electric will be subject to less regulation than that which currently exists. Instead, Staff and OPC presume that displacement of Missouri regulation by the SEC or the FERC would be ineffective or otherwise "detrimental to the public interest."

The Commission expanded upon the criteria used in evaluating acquisitions and mergers in Case No. EM-91-290, in the matter of UtiliCorp United and Colorado Transfer Company. As further explained in Western Resources, Inc and Southern Union Company, GM-94-90, 1993 Mo. PSC Lexis 42, the Commission stated:

> In Case No. EM-91-290, in the matter of Utilicorp United and Colorado Transfer Company, the Commission created a supplemental set of standards for acquisitions and mergers, those being:
>
> 'a. All documentation generated relative to the analysis of the merger and acquisition must be maintained.
>
> b. The company must present an estimate of the impact of the merger on its Missouri jurisdictional operations.
>
> c. The Company must provide an assessment of the relative risk regarding items that impact its Missouri operations.
>
> d. The Company must propose assurances or conditions that will address the overall merger components that pose the risk of being detrimental to the Missouri public interest.'

Id. The opinion in Case No. GM-94-90 does not indicate that continued Missouri Commission regulation of a utility following merger is in any way significant. Thus, it is apparent that whether or not the Commission may lose some direct regulatory authority to the FERC or the SEC has not in the past been considered as a reason to disapprove a merger.

C. Even where appropriately considered, "effective regulation" has not been limited to regulation by a particular agency.

Unlike the Missouri Commission, the FERC has long considered whether a proposed merger would impair effective regulation as

part of its determination whether the merger is "consistent with the public interest."[2] See Commonwealth Edison Co., 36 FPC 927 (1966), aff'd sub nom. Utility Users League v. FPC, 384 F.2d 16 (1966), cert denied, 393 U.S. 953 (1968). Even so, consideration of the "potential impairment of effective regulation has only infrequently been important in merger cases...." Midwest Power Systems, Inc. and Iowa-Illinois Gas and Electric Company, 71 FERC P 61, 386 (1995). Accordingly, the possible displacement of some state regulatory authority with FERC authority has not prevented the FERC from finding proposed mergers "consistent with the public interest."

In Entergy Services, Inc, the merger resulted in a reduction of state commission oversight. Entergy Services, Inc., 62 FERC P 61,073 (1993). The FERC, noting that this did not equate to a lessening of effective regulation, stated:

> [W]e acknowledge that if the merger is consummated, some degree of Federal preemption will come into play.... Power sales and transmission transactions among the public utility subsidiaries of the Entergy System, including Gulf States, if the merger is consummated, will be subject to this Commission's regulation. The fact that the Texas and Louisiana Commissions may need to address certain issues in [FERC] proceedings, as opposed to proceedings before them, does not mean that effective regulation will be diminished-- i.e., the fact that the forum to resolve certain issues will be at the [FERC], rather than before a state commission, does not suggest any diminishment of effective regulation.

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[2] This appears to be a higher standard than that used in Missouri where the merger must be approved "unless detrimental to the public interest".

Id., at 61,374. The FERC has even indicated that it had no difficulty with a certain degree of merger-related preemption of its own authority as a result of application of the SEC's jurisdiction:

> [W]ith respect to concerns that review of the particular affiliate transactions -- those covered in section 13 (b) of PUHCA -- may fall to the SEC and not this Commission, that fact does not dictate a finding of impairment of effective regulation.

Cincinnati Gas & Electric Co., 64 FERC P 61,237, 62,730-31 (1993). Instead of being a "critical" issue, as alleged by the Staff and the OPC, the potential limited displacement of some State regulation should play little, if any, role in determining whether the proposed merger is detrimental to the public interest. Moreover, based on the fact that Union Electric is willing to enter into agreements ensuring that to the extent possible the MPSC does not, on preemption grounds created by PUHCA, relinquish authority where it exists today, the above discussion may be unimportant to this proceeding. Clearly though, no basis exists for the Commission to deny approval of the merger merely because the SEC or the FERC may assume some regulatory responsibility currently exercised by the MPSC.

D. In determining whether a proposed merger is "not detrimental to the public interest", the Commission should not limit its focus to whether any Missouri Commission authority will be displaced, but instead should focus upon the unchallenged fact that ratepayers will experience billions of dollars in savings with no decrease in service reliability.

The standard used in considering this merger is whether it is "not detrimental to the public interest." State ex rel. City of St. Louis v. Public Service Commission of Missouri, 73 S.W.2d 393 (Mo. 1934). It is uncontradicted that the merger will result in substantial savings that will be shared with the Missouri ratepayers. Union Electric estimates that savings made possible by the merger extend into the billions of dollars. The economic benefits from the merger, considered alone, seemingly would make it impossible to conclude that this merger is detrimental to the public interest.

The Commission should not be distracted by the concerns expressed by the Staff and the OPC regarding limited federal preemption of some aspects of the merged companies business.[3] This is particularly true since UE is willing to enter into appropriate agreements to limit preemption under PUHCA to the extent possible.

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[3] It is difficult to judge the extent that preemption should be considered at all by the Commission. For example, active efforts are underway to repeal PUHCA, which some believe, will be successful in the next year or two.

III.
ABSENT AGREEMENT, THE SEC AND THE FERC WOULD PREEMPT MPSC JURISDICTION OVER CERTAIN ASPECTS OF THE MERGED COMPANIES OPERATIONS

A. Under the Ohio Power case, the SEC maintains primary jurisdiction over certain transactions for registered holding companies.

Provisions of PUHCA could potentially result in preemption of regulatory authority by the SEC over some areas presently regulated by the MPSC. Union Electric agrees with the Staff and the OPC that after Ohio Power Co. v. FERC, 954 F.2d 779 (D.C. Cir. 1992) a convincing argument can be made that, absent agreement to the contrary, the SEC has exclusive jurisdiction over inter-affiliate transactions under 15 U.S.C.A. §79*m*. Nonetheless, as in the CINergy cases, Union Electric believes that agreement may be reached permitting continued Missouri regulation in this area.

B. The FERC has primary jurisdiction over wholesale electric energy transactions by and between UE and CIPS.

It is well-established that the FERC has exclusive jurisdiction over wholesale energy transactions. See, Mississippi Power & Light v. Miss. ex rel. Moore, 487 U.S. 354 (1988). Ample precedent exists stressing the primacy of FERC authority over matters within its statutory jurisdiction and a state's inability to contradict that authority. See, Mississippi Power & Light, 487 U.S. at 374 (holding that "[s]tates may not regulate in areas where FERC has properly exercised its jurisdiction to determine just and reasonable

wholesale rates or to insure that agreements affecting wholesale rates are reasonable")(emphasis supplied); See also Id., at 377 (stating that "a state agency's 'efforts to regulate commerce must fall when they conflict or interfere with federal authority over the same subject'")(quoting Chicago & North Western Transportation Co. v. Kalo Brick & Tile Co., 450 U.S. 311, 318-319 (1981)). Accordingly, absent agreement by Union Electric Company, federal law would clearly apply to prevent Missouri regulation over areas of exclusive FERC jurisdiction.

IV.

NOTWITHSTANDING THE ABOVE, UNION ELECTRIC PROPOSES THAT THE PARTIES ENTER INTO A STIPULATION TO BECOME PART OF THE MERGER ORDER THAT PRESERVES, AS CLOSELY AS IS POSSIBLE TO THAT EXISTING PRIOR TO THE MERGER, MISSOURI COMMISSION AUTHORITY TO REGULATE INTER-AFFILIATE TRANSACTIONS, THE JOINT DISPATCH AGREEMENT AND SYSTEM SUPPORT AGREEMENT

Union Electric will briefly respond to proposed conditions submitted by the Staff and OPC pertaining to jurisdictional issues. For additional discussion of these proposed conditions, please refer to the testimony filed in this proceeding by UE witnesses D. Brandt and M. Borkowski.

A. Union Electric has proposed that, so far as is possible, the Missouri Commission not relinquish jurisdiction it may presently have.

Union Electric's position with regard to the jurisdictional issues raised by its reorganizing under PUHCA has been summarized as follows:

> The Company has agreed that Ameren Corporation and its subsidiaries will continue to be subject to MoPSC jurisdiction after the merger to the same extent that Union Electric Company and its subsidiaries and

> affiliates are subject to Missouri jurisdiction now. It is the Company's intent that, to the greatest extent possible, the MoPSC not lose any jurisdiction because of this merger, or the resulting corporate structure. However, the Company does not believe that it is appropriate for the Commission to be granted more jurisdiction over Ameren Corporation and its subsidiaries and affiliates than the Commission would have over Union Electric and its subsidiaries and affiliates or other utilities in Missouri, merely because of the merger.

(Testimony of Donald Brandt, pp. 10-12). Union Electric believes that it is appropriate to include language fulfilling the above principle in the order approving the merger, and, it is willing to work with appropriate parties to draft such language.

Nonetheless, the Company did have disagreement with some of the specific language contained in proposed conditions attached to the Staff Comments, as set forth more fully below.

A. Union Electric cannot accept, as drafted, conditions proposed by Staff in Attachment 1 to its Comments.

1. Paragraph 1:

This paragraph purports to establish MPSC authority over affiliate transactions that otherwise would pass to the SEC. Union Electric could agree to having affiliate transactions reviewable by the Missouri Commission on the same basis and to the same extent as other electric utilities not subject to PUHCA. No reason exists that Union Electric should be put to competitive disadvantage by agreeing to greater regulation in this area than that to which other utilities are subject. Thus, Union Electric would reserve all legal and equitable rights except the right to object to a decision of the MPSC on the basis that, under PUHCA,

the SEC has exclusive jurisdiction over registered holding company inter-affiliate transactions.

Next, since this paragraph deals only with inter-affiliate transactions, Union Electric believes that it would be entirely unnecessary to include language regarding this issue in all contracts. Clearly, Ameren and its affiliate companies would have notice of any agreement contained in the merger order.

Finally, Union Electric finds the last sentence of this section, if not incomprehensible, at least capable of several interpretations. Accordingly, it believes that this language should be omitted.

Consistent with the comments in this and paragraph 2, as well as the testimony, Union Electric would agree to submit the General Services Agreement for approval by the Commission.

2. Paragraph 2:

Union Electric cannot agree, simply by reason of the merger, to become subject to greater regulation than it or any other utility would otherwise be under the law. However, this paragraph apparently is such an attempt to assert greater regulatory authority than currently exists. Other utilities, even though they may have affiliates, are not subject to these types of rules.

The Commission has pending before it in Case No. OO-96-329 a proposed rulemaking applicable to affiliate transactions. In order to resolve this point, Union Electric would agree to comply with whatever rules are adopted in that docket, even though the

Company might otherwise be exempt from PUHCA. Further, UE would reserve all legal and equitable rights except the right to object to a decision of the MPSC on the basis that, under PUHCA, the SEC has exclusive jurisdiction over registered holding company inter-affiliate transactions.

3. Paragraph 3:

The Staff has proposed that Union Electric agree to submit to the Commission authority over "all wholesale electric energy or transmission service contracts...respecting...Union Electric Company" and any Ameren subsidiary or affiliate. (Emphasis supplied). The Staff's proposal seemingly requires this agreement with respect to not only contracts between UE and its affiliates but also to contracts with non-affiliates. This conclusion is reached on the basis of the word "respecting" in contrast with the use of "between" in the SEC related agreements described under the Staff's paragraph 1. Although possibly not intended by the Staff, it appears that this language would have the effect of expanding the current breadth of Missouri regulation to attempt to carve out new authority at the expense of the FERC.

The MPSC does not currently have authority to regulate wholesale contracts respecting Union Electric Company. This jurisdiction belongs exclusively to the FERC. Moreover, whether or not Union Electric merged, formed a registered public holding company or chose some other form of organization would not alter FERC jurisdiction in this respect. Mississippi Power & Light v.

Miss. ex rel. Moore, 487 U.S. 354 (1988). Thus, it is improper to attempt to condition approval of the merger on this requirement.

Nonetheless, Union Electric is willing to enter into an agreement, that to the extent legally permissible, preserves Missouri jurisdiction as it would exist but for PUHCA over the Joint Dispatch Agreement, the System Support Agreement, or other electric sales contract between Union Electric and an affiliated company. Union Electric notes that it is not aware of any case in which such an agreement has been upheld or approved.[4] However, without admitting that Staff is correct in its interpretation of the law, Staff did note that other possible avenues to maintain State control exist. (Comments, p. 8).

This paragraph contains language similar to the last sentence in Staff's paragraph 1. The language is objectionable for the same reasons as stated above. Further, Union Electric objects to including language regarding preemption in all contracts as this is unnecessary and unduly burdensome.

4. Paragraph 4:

This paragraph, too, appears to be an attempt to expand Commission jurisdiction beyond that which presently exists. The FERC currently has exclusive jurisdiction over gas contracts for interstate natural gas related services respecting Union Electric. The Company does not object to attempting to preserve

[4] The CINergy cases, cited by OPC, concerned agreements regarding SEC jurisdiction under PUHCA, not FERC jurisdiction.

jurisdiction that currently exists to the extent possible. However, some preemption of State authority presently exists in this area. (See, American National Can Co. v. Laclede Gas Co., 30 Mo.P.S.C. (N.S.) 32 (1989) and In the Matter of Missouri Public Service Company, 30 Mo.P.S.C (N.S.) 39 (1989), where the preemption doctrine was thoroughly analyzed and accepted by the Commission in refusing to bar recovery by gas utilities of FERC approved take-or-pay charges billed by interstate pipeline suppliers.) The Company does not agree that the fortuitous happening of the merger provides an opportunity to overturn these established principles of FERC preemption.

Union Electric has the same objections as in paragraph 3 above regarding including preemption language in contracts. In this regard, it must be noted that many of the gas supply contracts are not capable of being amended by Union Electric in the manner suggested. The constraints are addressed in UE witness Borkowski's surrebuttal testimony, pp. 29-30).

B. The Company will agree to make records and personnel available for the Commission.

Both the Staff and the OPC express concern regarding the access of books and records by UE, Ameren or other affiliates. However, neither the Staff nor the OPC discussed in their memorandum the 1992 amendments to Federal Power Act, 16 U.S.C.A. §824 (g), which permit access to books and records of affiliates, holding companies and other entities. This provision would adequately protect the ability of the Commission to perform its regulatory function.

Even so, Union Electric is agreeable to making books, records and personnel available for review by the Commission to the same extent as is the current practice. In other words, Union Electric will not seek to limit access to books, records and personnel solely by reason of PUHCA.

C. Merger approval cannot be conditioned on acceptance by the SEC or the FERC of conditions designed to preserve State regulatory authority.

The Staff and the OPC suggest conditioning approval of the merger on the FERC and the SEC accepting conditions designed to preserve (or expand) Missouri Commission authority. Union Electric does not believe such a condition to be either legal or wise.

For all the reasons noted above and in testimony, it is extremely doubtful that the possible preemption of some part of the Commission's regulatory authority by the SEC or the FERC could be found to outweigh the enormous economic benefit to customers so as to provide a basis to disapprove the merger. This is especially true, since Union Electric, in forming a public utility holding company is not breaking any law or doing anything which is capable of being portrayed in a negative light. Rather, it is exercising its rights under long-existing federal law to organize its business in a certain fashion.

Union Electric is willing to do what it can to preserve Missouri authority where this can be accomplished. However, it is unwise and unfair in the extreme to put at risk billions in savings for Missouri customers solely in support of the already

fractured principle that Missouri Commission authority can never be preempted.

IV.
RECOVERY OF TRANSACTION EXPENSES FOR 1995 DOES NOT CONSTITUTE RETROACTIVE RATEMAKING

Staff has objected to the recovery of approximately $9 million in transaction costs incurred in 1995 solely on the basis that recovery might constitute retroactive ratemaking. (Imhoff Testimony, pp. 6-10). Union Electric has addressed these concerns in the testimony of Warner Baxter. (Baxter Testimony, pp. 1-8). Union Electric strongly objects to the Staff's position on this issue and believes it to be demonstrably incorrect. However, Union Electric will address these issues in greater detail in a future legal memorandum or brief.

Respectfully submitted,

UNION ELECTRIC COMPANY

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