BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Union Electric Company d/b/a Ameren Missouri's Tariffs to Increase its Revenues for Electric Service	)))	**Case No. ER-2012-0166**

INITIAL POST-HEARING BRIEF OF THE OFFICE OF THE PUBLIC COUNSEL

OFFICE OF THE PUBLIC COUNSEL
Lewis R. Mills, Jr. (#35275)
Public Counsel
Christina L. Baker (#58303)
Senior Public Counsel
Missouri Office of the Public Counsel
P.O. Box 2230
Jefferson City, MO 65102-2230
(573) 751-4857
(573) 751-5562 FAX

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I. INTRODUCTION

This brief will address the following issues as identified in the List of Issues:

1. Plant in Service Accounting
2. Rate Case Expense
3. Return on Equity (including Regulatory Policy and Economic Considerations)
4. FAC Tariff
5. Class Cost of Service, Revenue Allocation and Rate Design

Many of the issues in the case were resolved through a series of agreements, and Public Counsel does not currently have the resources to delve into the remaining issues. Public Counsel reserves the right to address additional issues in its reply brief.

II. PLANT IN SERVICE ACCOUNTING

Plant in Service Accounting is Ameren Missouri's latest gimmick in its ongoing attempt to fundamentally change the regulatory process because regulatory lag is at the moment working against shareholders. Plant in Service Accounting is a concept that Ameren Missouri invented just for this case. Much like its recent proposal to implement part of its requested rate increase as an interim rate increase, and its continuing efforts in the legislature to get the statutory timeline for rate cases shortened, Ameren Missouri seeks Plant in Service Accounting simply to get more money (or get money faster) for shareholders.

With respect to the Plant in Service Accounting proposal (and similar proposals to implement some type of extraordinary accounting treatment), the first question the Commission should ask is: "Are the items for which the utility seeks extraordinary accounting treatment really extraordinary items?" There are two aspects to the determination of whether the items are

extraordinary: whether the items themselves are truly out of the ordinary, and whether the financial impact of accounting for the items in the ordinary way would have an extraordinarily deleterious effect. A corollary question is: "Has something fundamentally changed such that the normal process of addressing all costs in a general rate case has become inadequate to deal with these particular costs, and such that the Commission must create or authorize extraordinary treatment?"

As this Commission has long recognized: "Lessening regulatory lag by deferring costs is not a reasonable goal unless the costs are associated with an extraordinary event."[1] Ameren Missouri conceded that the expenditures that would be subject to Plant in Service Accounting are not outside of the Company's control, are not volatile, and are not unpredictable. (Transcript, pages 621, 657) Ameren Missouri also conceded that the Company's situation of not earning its authorized rate of return (the premise on which the Plant in Service Accounting scheme is based) is not extraordinary. (Transcript, page 656)

If the Commission views Ameren Missouri's novel Plant in Service Accounting concept in light of these kinds of basic questions, it will come to the conclusion that the Plant in Service Accounting mechanism is neither necessary nor warranted. The utility business model has not fundamentally changed, the economy has not fundamentally changed, and process of replacing plant has not changed. While nobody involved in the process particularly likes general rate cases, they are the best way we have to address a utility's costs and rates in a holistic manner. Indeed they may very well be the only way; certainly no utility in Missouri has proposed a reasonable alternative. The answer is not to create mechanism after mechanism by which

[1] In re Missouri Public Service Co., Case Nos. EO-91-358 & EO-91-3601, 1 Mo. P.S.C. 3d 200, 207 (1991)

increasing costs are automatically addressed and declining costs – or perhaps more importantly, areas where costs could be declining but aren't – are not examined.

Ameren Missouri witness Lynn Barnes is the originator of the Plant in Service Accounting concept. (Transcript, page 582) She defines Plant in Service Accounting as:

> Plant-in-Service Accounting refers to regulatory treatment which would allow for the accrual of return and the deferral of depreciation expense during the period between when nonrevenue-producing assets are placed in service and the point when they become part of rate base following a rate case, offset by retirements and changes to the accumulated depreciation reserve. (Exhibit 11, Barnes Direct Testimony, page 16)

Public Counsel opposes the Company's Plant in Service Accounting proposal. Public Counsel witness Robertson summarizes some of the reasons for this opposition in his Direct Testimony:

> [T]he Company seeks to isolate one component (plant) in its cost of service calculation, while ignoring other components within the same cost of service calculation. Revenue could increase, operating expense could decline and other rate base items in addition to individual components within plant-in-service and accumulated depreciation could decline. These items are also exposed to regulatory lag. The premise behind observing a test year for audit purposes (and true-up if needed) is to match revenue and cost of service during a specific period to ensure calculation of a revenue requirement that is fair to both the Company and to ratepayers. (Exhibit 406, Robertson Direct Testimony, pages 5-6)

Ms. Barnes testified that Ameren Missouri considers it irrelevant that no other state has adopted the Plant in Service Accounting mechanism. (Transcript, page 581) Public Counsel submits that, while such novelty is not determinative, it is certainly relevant. The fact that no jurisdiction anywhere has ever adopted such a mechanism should at least cause the Commission to give the proposal very careful scrutiny here.

Moreover, not only has no jurisdiction ever adopted the mechanism, it has never been written up in any authoritative text on utility ratemaking. (Transcript, page 582) It has never been mentioned in a treatise. (Transcript, page 582) It has never been the subject of a journal

article. (Transcript, page 582) It has never been ruled upon in a court case. (Transcript, page 583)

Reflecting the fact that utility proposals to change the regulatory framework are one-sided in favor of shareholder returns – generally as well as specifically with respect to Plant in Service Accounting – the Plant in Service Accounting proposal can only operate in one direction: in favor of shareholders. It can only serve to increase costs to ratepayers; it is mathematically impossible for it to ever favor ratepayers. (Transcript, page 584) And Ameren Missouri has never made a proposal, neither a general proposal nor a specific proposal, that would try to capture increased revenues from revenue-producing assets in between rate cases. (Transcript, pages 583-584)

All of the structural changes to the regulatory framework in Missouri in recent years have been what Public Counsel has referred to as regulatory ratchets: they generally only work in one direction (against ratepayers), and once they have been tightened down on ratepayers, they never loosen up. The Plant in Service Accounting scheme is a perfect example: it is designed to fundamentally change the regulatory paradigm in favor of shareholders, it cannot ever work to benefit ratepayers, and one can be sure that if utilities ever convinced the Commission to adopt it, they would never give it up. In addition, no matter how many times a utility has increased the pressure, it seems to always be ready to tighten the ratchet another notch. As Chairman Gunn noted (Transcript, pages 649-652), the Commission has recently made a number of concessions to Ameren Missouri in terms of trackers, a fuel adjustment clause, accounting authority orders, and similar exceptions to the regulatory framework, but here is Ameren Missouri in this case seeking yet another mechanism, a newly-minted one created just for this case. Even though the clear implication is that all the previous concessions are not sufficient, Ameren Missouri is

certainly not proposing to give any of them up; that's not how the ratchet works. It can only get tighter, never looser.

Ameren Missouri freely admitted that the Plant in Service Accounting proposal is a way to get ratepayers to be investors in Ameren Missouri's system. (Transcript, page 585) But rather than getting an actual return for being compelled to invest, they merely get reliable service. (Transcript, page 585) Safe, adequate and reliable service is not something that ratepayers should have to pay extra for; it is what Ameren Missouri is required to provide under the regulatory compact. According to that compact, in exchange for a monopoly service territory and a guaranteed opportunity to earn a fair return on shareholder investment, a utility is obligated to provide safe, adequate, and reliable service to all customers. Nothing in the regulatory compact requires ratepayers to become involuntary investors.

Another problem with the Plant in Service Accounting proposal, and it may be due to the concept having just been dreamed up for this case, is that it is not fully fleshed out. Staff witness John Cassidy noted that the company really has not offered any explanation for how or what non-revenue-producing investments should be included. At the hearing, he noted as an example a large transmission line that does not produce additional revenue from native load customers, but might enable additional off-system sales. (Transcript, page 743) It is not clear whether this type of investment would be included, and the lack of clarity would inevitably lead to the need to sort out such issues in succeeding rate cases, which would create a significant burden on the Staff and other parties. (Transcript, page 744)

Perhaps one of the most shocking and scariest concessions in the entire evidentiary hearing was Ms. Barnes' frank admission that, if the Commission allows Plant in Service Accounting, rates will be going up even more than they already are. (Transcript, page 586)

Anyone concerned with the skyrocketing rate increases that we have already experienced, and Ameren Missouri's calm and confident predictions that there are more to come, should run away screaming from the Plant in Service Accounting proposal that will escalate the problem. And it will not cause small additional increases, either. Allowing Plant in Service Accounting **in just one case** could increase rates by $240 million over the course of forty years. (Transcript, page 675) If the Commission were to allow Plant in Service Accounting in multiple cases, that $240 million would be multiplied by however many times the Commission allowed it.

Luckily for ratepayers, Ameren Missouri witness Barnes also conceded that the Plant in Service Accounting mechanism is not necessary unless the Commission finds two specific problems: 1) that regulatory lag is excessive; and 2) that Ameren Missouri is currently under-investing in its system. (Transcript, page 591) Public Counsel is confident that the Commission will have little difficulty in rejecting both of these premises.

Part of Ameren Missouri's justification for its Plant in Service Accounting proposal is that it is not logical to have a return (AFUDC, or Allowance for Funds Used During Construction) on plant before it is in service and a return on that plant after a rate case, but no return on the same piece of plant during the gap between the date it is placed into service and the effective date of new rates in the rate case following the in-service date. But Staff witness John Cassidy explained why it is in fact logical to have a potential gap:

> Once it's in service, then the – the construction has stopped and so there's no longer a need to continue to accrue AFUDC on that construction.
>
> …
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> Then at that point it's incumbent upon the company to determine whether it needs to file a rate case to address those costs that they've put into service.
>
> …
>
> [It is] the company's decision. It's in their control. (Transcript, pages 740-741, 764)

MIEC (Missouri Industrial Energy Consumers) witness Michael Brosch also addressed

the Company's concerns about this "gap," and like Staff witness Cassidy, found those concerns to be grossly overstated. He noted:

> [A]t the time construction is completed, the asset is eligible for consideration in rate base. Given the dynamic environment that occurs between test years, there's a continue -- a continual process of building new plant, retiring old plant. Everything's very dynamic.
> So you can't say that a specific asset that was completed in August of 2012 is not being allowed to earn a return. An overall revenue requirement is being established in this case that may be sufficient to pay a return on all the new assets added for the next two or three years.
>
> …
>
> [I]f you look for explicit recognition and inclusion of a particular asset, yes, you have that regulatory lag phenomena to consider. The bigger issue is holistically is the overall revenue requirement sufficient to provide a return on completed new construction net of retirements of old plant and all the other changes.
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> …
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> You know, I don't think it's the problem that you've made it out to be. I think that, as I said, you look at Mr. Weiss' calculations and rate base is relatively stable but for the Sioux scrubber addition.
> What you see is volatility in the income statement that suggests that **an inability to contain expenses** at the same rate of growth that revenues are growing is really the root cause of the historical earnings problem. (Transcript, pages 801-803; emphasis added)

III. RATE CASE EXPENSE

The Commission should not require already-beleaguered ratepayers to pay the $2 million that the Company estimates it will spend primarily on high-priced outside experts and outside attorneys. The Commission, from its questions in this case and in previous rate cases, seems troubled by disallowing an actual expense that the Company has incurred, particularly because it is associated with a necessary part of the regulatory process. But the Commission should note that past Commission had similar questions about disallowing similar expenses like executive compensation and advertising. Despite those initial questions, past Commissions understood that

portions of executive compensation expense and portions of advertising expense, while legitimate costs of doing business, serve primarily to benefit shareholders rather than ratepayers. Past Commissions disallowed executive compensation expense, past Commissions disallowed advertising expense, and both of these types of disallowances are now an accepted part of the regulatory framework in Missouri. There is no statutory reason why this Commission cannot extend the reasoning that applies to executive compensation and advertising disallowances to rate case expenses. Just as the Commission routinely disallows executive compensation expense unless a utility can show that such expense directly benefits ratepayers, and just as the Commission routinely disallows advertising expense unless it is of a type that directly benefits ratepayers, so too should this Commission disallow rate case expense unless the Company can show that it directly benefits ratepayers.

In his direct testimony, Public Counsel witness Robertson explained Public Counsel's position on rate case expense:

> Costs associated with a general rate increase case should first be analyzed to determine if they are prudent, reasonable and necessary. Those that are determined not prudent, reasonable or necessary should not be reimbursed by ratepayers. For example, costs incurred by Company personnel, outside legal and outside consultants that are determined imprudent, unreasonable or unnecessary should be automatically disallowed. In addition, if the utility has employees capable of developing and supporting the general rate increase case, the cost of hiring higher-priced outside legal counsel or consultants should not be allowed either. (Exhibit 406, Robertson Direct Testimony, page 10)
>
> The response to MPSC Data Request No. 59, indicated that as of September 30, 2011 Ameren Missouri employed 4,321 regular full-time employees, Ameren services employed 1,308 regular full-time employees and Ameren Corporation as whole employed 9,130 regular full-time employees. OPC believes it reasonable to assume that since many of these same employees hold degrees from colleges and universities which likely match or exceed the educational requirements needed to prepare and defend a general rate increase case - not to mention their combined work experience and acquired skills. These employees should be able to perform most, if not all, of the work required…. Company's response to OPC Data Request No. 1008 and 1008s identified 15 licensed attorneys employed by

Ameren. Of the 15 identified, 8 possess current regulatory practice experience. (Exhibit 406, Robertson Direct Testimony, pages 15, 16)

Mr. Robertson further testified that Ameren Missouri and its affiliates employ hundreds of highly educated employees holding a bachelor degree or higher in many different areas relevant to the rate case disciplines. (Exhibit 406, Robertson Direct Testimony, page 18)

Mr. Robertson also testified that, once the Commission determines the appropriate level of rate case expense (taking into account the ability of in-house personnel to perform the required work), this level of expense should be fairly apportioned between ratepayers and shareholders since both groups benefit from rate cases. (Exhibit 406, Robertson Direct Testimony, page 19) Clearly, shareholders benefit from rate cases; the Company freely admits that they do. (Transcript, page 867) The concept of shareholders absorbing a portion of a utility's cost of doing business is not unique to rate case expense.

The Commission has regularly required costs of executive compensation to be excluded from rates if the criteria for awarding that compensation do not appear directly tied to ratepayer benefits.[2] The analogy to rate case expense is compelling. Both incentive compensation and rate case expense have the potential to benefit shareholders much more than to benefit ratepayers. Both certainly have the potential to become very significant expense items, and indeed have

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[2] At the hearing (Transcript, page 848), Commissioner Kenney asked for citations to cases in which the Commission had disallowed executive compensation on the theory that such compensation provided more benefit to shareholders than to ratepayers. Although there are many such decisions, the most recent Commission decisions appear to be in two recent Kansas City Power & Light Company cases:
In re Kansas City Power & Light Company, Commission Case No. ER-2006-0314, 15 Mo PSC 3d 138, 171-172, Report and Order (December 21, 2006).
In the Matter of the Application of Kansas City Power & Light Company for Approval to Make Certain Changes in its Charges for Electric Service to Implement its Regulatory Plan, Case No. ER-2007-0291, 2007 Mo. PSC LEXIS 1438, pages 75-81, Report and Order (December 6, 2007)
Note that the cited portion of the latter decision includes references to several other, earlier decisions.

done so.

Rate case expense can also be analogized to advertising expense, some of which is routinely excluded from rates. In fact, so routine is the inclusion that utilities generally remove some advertising expense voluntarily, and Ameren Missouri did so in this case. (Transcript, page 876) The fact that the Commission is within its statutory authority to exclude some advertising expense is well-settled law in Missouri. The Court of Appeals, Western District, held so in a Laclede Gas Company rate case appeal in 1980:

> While it is correct that utilities operate within our free enterprise system, the courts remain mindful that these same utilities are, in fact, by their nature monopolies. The history of regulation of such monopolies has been one of a continued balance between preserving the existence and integrity of the utility so it might continue service to the users, and protection to the users and ultimate ratepayers against unwarranted costs for utility services.
>
> From the authorities considered upon this point, certain principles emerge, which permit disposition of this issue. It is obvious that the P.S.C. has no authority to take over the general management of any utility. It is just as obvious that a utility is a person under our laws entitled to all the constitutional safeguards as to free speech provided for under the first amendment to the United States Constitution and made applicable to the states by the 14th amendment.
>
> …
>
> The P.S.C. gave specific attention to the nature and extent of the advertising in question. The evidence is competent and substantial to support the finding of the P.S.C. that costs of advertising related to safety, off-peak usage and conservation are proper cost items to be included within the rate schedule.
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> …
>
> The order of the P.S.C. does not prohibit advertising by Laclede. If it had, this order would, without question, have violated the constitutional and managerial rights of Laclede. What the order prescribes is that advertising **cost items directly related to the benefit of ratepayers are justified operational costs permitted to be included within the rate schedule. All other such expenses, while they too are decisions of management, are not operational costs includable in the rate schedule.**
>
> This court is persuaded that § 393.140(5) and § 393.270(4), RSMo 1978 authorize the P.S.C. to examine the methods, practices, regulation and property employed by public utilities, and that such authorization extends to examination of advertising cost. This court finds of particular persuasion the case of State of Oklahoma v. Oklahoma Gas and Electric Company, supra, at 894, in that it adopts the principle therein when it states: "We conclude the Commission may disallow any institutional advertising expenditures from operating expenses for ratemaking

> purposes **unless the utility establishes** such expenditures benefit all ratepayers." By the adoption of such a rule, the managerial prerogatives of Laclede are maintained, and the right of Laclede to continue to exercise its right of free speech is preserved, while at the same time the P.S.C. can perform its regulatory role of balancing the integrity of regulated utilities against the protection of the ratepayer.
>
> This court concludes that pursuant to the statutory authority cited herein, denial of certain advertising costs was lawful and further, there was substantial and competent evidence that the finding of the P.S.C. was reasonable.[3]

Public Counsel's position in this case is very similar to the analysis provided by the Court of Appeals in Laclede. Public Counsel asserts that the Commission should not allow the expenses attributable to high-priced outside experts and outside attorneys unless the Company can show that ratepayers benefit from such expenses, just as the Court found that the Commission may disallow any institutional advertising expenditures from operating expenses for ratemaking purposes **unless the utility establishes** that such expenditures benefit all ratepayers. Public Counsel is not asserting that the Commission should forbid Ameren Missouri from using whatever witnesses and attorneys it desires to use, because that would be unlawful just as it would be for the Commission to forbid Ameren Missouri to undertake certain types of advertising. But the Commission not only can, but must, disallow rate case expenses that do not benefit ratepayers. Failure to do so would be a failure to provide "protection to the users and ultimate ratepayers against unwarranted costs for utility services."[4]

One of the problems that the Commission's practice of generally including all rate case expense unless a party has made an iron-clad demonstration of imprudence has caused is that the

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[3] State ex rel. Laclede Gas Co. v. Public Service Com., 600 S.W.2d 222, 228-229 (Mo. Ct. App. 1980); emphasis added. Commissioner Kenney's question referenced in footnote 2 also encompassed advertising, and Public Counsel believes that this citation is directly responsive to that portion of the question. Because the appellate decision so clearly established the Commission's authority, there are relatively few recent Commission cases in which advertising expense has been litigated, and the recent cases have to do with the appropriate classification of costs, not whether certain advertising costs may properly be excluded from rates.

[4] *Ibid*., at 228.

Company has little incentive to control rate case costs. During the hearing, there were occasions when a number of attorneys representing Ameren Missouri were spending unproductive time in the hearing room. (Transcript, pages 834-835) Much more troubling was the admission of the Company's Controller that she was making little effort to track – much less control – the accumulation of rate case expense. (Transcript, pages 855-856) She testified that nobody in management had **ever** asked her how many hours in-house personnel were spending on the rate case. (Transcript, page 857) Moreover, if they had bothered to ask, she doesn't know the answer. (Transcript, page 857) Clearly, Ameren Missouri has insufficient incentive to keep rate case expenses low.

IV. RETURN ON EQUITY

Public Counsel's position on this issue is reflective of the specific economic considerations Ameren Missouri's customers are currently facing, and is consistent with the United States Supreme Court's guidance in the seminal cases of Hope and Bluefield.[5] Public Counsel asserts that once the Commission has determined a just and reasonable Return on Equity (ROE) range, it must order that rates be set at the low end of the range in this case in order for rates to be just and reasonable for Ameren Missouri's customers.

The charge of the Commission is to set rates that are just and reasonable. An important part of a just and reasonable rate is an authorized return on equity that is neither excessive nor confiscatory. (Transcript, page 1575) A reasonable return on equity, as developed by the United States Supreme Court decisions in the Hope and Bluefield cases, is: (1) adequate to attract capital at reasonable terms, thereby enabling Ameren Missouri to provide safe and reliable electric

[5] Bluefield Waterworks and Improvement Co. v. Public Service Commission of West Virginia, 262 U.S. 679 (1923); Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591 (1944).

service; (2) sufficient to ensure Ameren Missouri's financial integrity; and (3) commensurate with returns on investments in enterprises having corresponding risks. The experts for Ameren Missouri, MIEC and Staff agree that a ROE that meets all those requirements would be reasonable and not detrimental to Ameren Missouri. (Transcript, pages 1571, 1698, 1970-1971)

The Commission cannot arrive at an appropriate rate of return on equity without considering the point of view of the ratepayers. Even Ameren Missouri Chief Executive Office Warner Baxter agreed that the determination of just and reasonable rates must be looked at from all perspectives, including the customers' perspective. (Transcript, page 259) Mr. Baxter reiterated several times that the Commission should take into account all the testimony from all the local public hearings when deciding on the level of the rate increase granted in this case. (Transcript, pages 259-261) Mr. Baxter was unable to suggest a specific way that the Commission should take that testimony into account, but he acknowledged that the proposal made by Public Counsel witness Meisenheimer is a possible approach. (Transcript, page 261)

Multistage DCF analysis, constant growth DCF analysis, CAPM, and the bond yield risk premium are all methodologies commonly used by rate of return witnesses and capital market specialists in estimating the cost of equity. (Transcript, page 2028) Mr. Murray, Mr. Gorman and Mr. Hevert are all experts in their fields. (Transcript, pages 1573-1574, 1617-1618, 1764, 2014, 2015) Their determinations were based on expert analysis of market-driven data using these traditional analytical tools. (Transcript, page 1970) However, Mr. Hevert is the only witness with a recommended ROE range above 10% (or for that matter, the only one with a recommendation above even 9.5%). Using the same methodologies, MIEC witness Mr. Gorman states that his calculations show that a ROE anywhere between 9.2% and 9.4% would be reasonable for Ameren Missouri. (Transcript, pages 1699, 1711) Similarly, Staff witness Mr.

Murray has calculated a reasonable range for ROE anywhere between 8.00% and 9.00%. (Transcript, page 1972) It is no surprise that given the inputs that Ameren Missouri's expert chose for his study that his results show the highest ROE reasonable range. (Transcript, page 1695) The other experts have responded to Mr. Hevert's ROE studies and believe that he has overstated a fair return on equity for Ameren Missouri in this case. (Transcript, page 1695; Exhibit 229; Exhibit 230; Exhibit 509)

Ameren Missouri's recommendations do not reflect the market realities today. Since 2005, the overall cost of capital has gone down. (Transcript, pages 1563-1565, 1691) The cost of equity has also gone down since the last rate case. (Transcript, pages 1548-1549) Utility bond yields have declined. (Transcript, pages 1551, 1563, 1693; Exhibit 529) Overall Treasury bond yields have declined. (Transcript, pages 1550, 1563, 1593, 1692-1693, 1765) As a result, average ROE awards for electric companies throughout the country have declined. (Transcript, page 1553-1556; Exhibit 530) Even the recommended ROE by the Company has gone down between the time the direct case was filed and today. (Transcript, page 1593)

ROE awards are not increasing. (Transcript, page 1604) Mr. Gorman even stated that if return on equity estimates stay as low as some of his studies have indicated, he eventually will be recommending return on equities lower than he is now. (Transcript, pages 1774-1775) But that has not stopped Ameren Missouri from recommending a ROE that is more than its current authorized return on equity of 10.2%. (Transcript, pages 1592, 1767) Ameren Missouri witness Mr. Hevert recommends a range for ROE of 10.25% to 11.00% with a recommendation that the Commission approve 10.5% for use in this case. (Transcript, page 1569) Contrary to the current market environment, even the bottom of Mr. Hevert's reasonable range for ROE is higher than Ameren Missouri's current authorized ROE.

Fluctuations in the economy are a normal part of the business arena, and this fluctuation is a part of doing business. (Transcript, page 1970) What is relevant in this case is what the current market cost of equity is for Ameren Missouri not what their last authorized return on equity was. (Transcript, page 1768) If the utility has a right to expect the Commission to increase its return on equity in a rate case, then customers have the right to expect the Commission to decrease the return on equity in a rate case if the evidence suggests it is the fair thing to do. (Transcript, page 1768)

Ameren Missouri would have the Commission believe that the Company would somehow be seen as riskier and less able to attract capital at more favorable rates if the ROE it receives is not the same or greater than it received in its previous rate case. Ameren Missouri hints that its credit ratings are in peril. But credit ratings are based on a mix between the business environment and a company's financial risk. (Transcript, page 1530) It is true that a basic tenant of finance is the risk-return trade-off so that investors require a higher return for more risky investments. (Transcript, pages 1711-1712) However, utilities are less risky and typically have beta coefficients (a measure of the relative volatility of a stock) of less than one. (Transcript, page 1577) Utility stocks are less volatile than the overall market and, therefore, less risky than the overall market. (Transcript, page 1577) It would be reasonable to expect that in the economy today, as a regulated monopoly with much lower risk, Ameren Missouri would have returns that are lower than a Fortune 500 company would have. (Transcript, page 1694) Mr. Murray testified that the mere fact of authorizing a higher ROE, and a resulting higher dollar rate increase, does not necessarily change the risk profile of the company. (Transcript, page 2015) In fact, right now Ameren Missouri's earned ROE is in the 7 percent range, which supports cash flow metrics in the benchmark for a BBB rating from Standard and Poors.

(Transcript, pages 2018, 2022) The only reason Ameren Missouri has a current BBB- rating is due to its non-regulated affiliate, not the actions or awarded ROE of the regulated utility. (Transcript, page 2018, 2022) Therefore, the business environment has more to do with the current downgrade to a BBB- than the financial risk of the regulated utility.

Ameren Missouri would also have the Commission believe that one consideration in its request for a higher ROE is a seemingly riskier regulatory environment in Missouri. (Transcript, pages 1626-1627) But the evidence shows that Missouri is far from a risky regulatory environment for Ameren Missouri. If authorized returns on equity were consistently too low, one would expect to hear credit rating agencies being critical of regulatory Commissions' authorized returns - but such is not the case. (Transcript, page 1704) Credit rating agencies are rating the utility industry (including Ameren Missouri) as stable, indicating that regulatory treatment is supportive of credit standing, which includes fair compensation and the ability to maintain adequate access to capital. (Transcript, pages 1704-1705) Thus market evidence suggests that the way things are being done by state commissions, including the Missouri Commission, is accomplishing the overall objective. (Transcript, page 1705) From a consumer perspective, Ameren Missouri has received a large number of concessions including regular rate increases, reduced risk as a result of the FAC and more extensive use of surcharges, trackers, and other extraordinary rate-making mechanisms that enhance the profit of shareholders. (Exhibit 402, page 9) For example, in Missouri rate cases utilities get their rate base actually stated as of a true-up date rather than on an averaged or forecasted rate base, which is more favorable to the utility because it produces a higher revenue requirement. (Transcript, page 1696-1697, 1705-1706) Even Mr. Hevert agrees that the Commission has instituted policies and designs that have been helpful to the company and that it is fair and appropriate that those should be taken into

consideration. (Transcript, page 1627)

In the current case, the Commission should also focus on ensuring rate affordability and fairness for consumers. In addition to cost of service, other relevant factors to consider in setting just and reasonable rates include the value of a service, the affordability of service, rate impacts, and rate continuity. (Exhibit 402, page 3) Part of determining a reasonable rate is to make rates as affordable as possible without causing a detriment to the utility. Customers testifying in public hearings and customers submitting comments to the Commission have regularly voiced frustration and concern about the burden of additional rate increases given the state of the economy. (Exhibit 402, page 9; Transcript Volumes 1-16)

Public Counsel urges the Commission to decide issues in a manner that recognizes the economic challenges faced by households in Ameren Missouri's service area and reasonably minimizes the rate impact on consumers. (Exhibit 402, pages 2-3) Once the Commission has determined a just and reasonable ROE range, Public Counsel requests that the Commission order the low end of the range in this case to promote affordability for Ameren Missouri’s customers. An awarded ROE that is anywhere within a just and reasonable range is neither excessive nor confiscatory. Just because the experts may have recommended a specific ROE does not mean the entire range they have supported is not reasonable. Mr. Hevert’s range for ROE is from 10.25% to 11.00% so if the Commission ultimately orders a ROE anywhere within his range, he would consider that to be reasonable. (Transcript, pages 1629-1630) MIEC witness Mr. Gorman states that his calculations show that a ROE anywhere between 9.2% and 9.4% would be reasonable for Ameren Missouri. (Transcript, pages 1699, 1711) Similarly, Staff witness Mr. Murray has calculated a reasonable range for ROE anywhere between 8.00% and 9.00%. (Transcript, page 1972) While his recommendation may be higher, Mr. Hevert admits that the

lower end of his ROE range, or 10.25%, would satisfy the Bluefield and Hope standards set by the U.S. Supreme Court for a reasonable ROE. (Transcript, page 1576) The same is reflected in the testimony of Mr. Murray and Mr. Gorman.

The effect of ROE on the customers and the affordability of rates in this case is staggering. According to Staff's Reconciliation (Exhibit 409), the Total Revenue Requirement increase expressed by the Company at True-Up would be $345,256,729 if the Commission approves the Company's recommendation for 10.5% ROE. If the Commission approves the top of Staff's recommended range of ROE, or 9.00%[6], the Company's revenue requirement would be reduced, an annual saving to customers of $83,192,181 (approximately 24%). If the Commission approves the bottom of Staff's recommended range of ROE, or 8.00%, the Company's revenue requirement would be reduced and annual savings to customers would be $147,341,010 (approximately 43%). All of the ROEs reflected in Staff's Reconciliation have expert testimony behind them stating that they satisfy the Bluefield and Hope standards set by the U.S. Supreme Court for a reasonable ROE. The lower the approved ROE, the more affordable the rates are to the customers. Therefore, Public Counsel asks that once the Commission has determined a just and reasonable ROE range, that it order rates be calculated based upon the low end of the range in this case to promote affordability for Ameren Missouri's customers.

Public Counsel witness Meisenheimer's recommendation with respect to ROE is the **only** proposal in the case that takes into account the testimony adduced at the local public hearings. The Company readily agreed that the Commission should consider this testimony when it decides how much of a rate increase to grant in this case (Transcript, pages 259-262), but did not advance any proposal for doing so. If the Commission does not adopt Public Counsel's

[6] Which is very close to the bottom of MIEC's recommended range of 9.2%.

recommendation to award an ROE at the bottom of the reasonable range, it will have effectively ignored the testimony of all the witnesses who testified at all the local public hearings.

V. CLASS COST OF SERVICE AND RATE DESIGN

On October 10, 2012, many of the parties filed a Non-Unanimous Stipulation and Agreement regarding class cost of service and rate design. No party opposed the agreement, and as a result of the items agreed to, the only outstanding issue with respect to class cost of service and rate design is Ameren Missouri's proposal to increase all customer charges for residential and small general service classes by 150%. Public Counsel opposes this drastic increase for the reasons set forth in this section of this brief. In general, those reasons are: 1) the proposed increase is not supported by valid cost studies, because the Company's study includes many inappropriate costs as customer-related, and the Staff's cost study includes inappropriate levels of energy-related bad debt; 2) the Company has failed to adequately analyze the effect of its proposal on low income and low usage customers; and 3) the Company has refused to acknowledge the impact of increasing customer charges on customers' energy efficiency efforts.

Public Counsel witness Meisenheimer explained the basis for Public Counsel's position on customer charges in her direct testimony:

> My CCOS studies suggest the average customer cost recoverable in a customer charge is a little under $6 for the Residential class and about $10.65 for the Small General Service Class. I do not anticipate significant changes in these calculations in future study updates. The current customer charges exceed these costs so I recommend that there be no increase in the Residential or SGS customer charges in this proceeding. (Exhibit 402, Meisenheimer Direct Testimony, page 17)

In his surrebuttal testimony, Public Counsel witness Ryan Kind discussed additional

reasons to refrain from raising the residential customer charge. Commenting on the rebuttal testimony of Natural Resources Defense Council (NRDC) witness Pamela Morgan, Mr. Kind stated:

> Public Counsel agrees that the substantial increases in customer charges proposed by UE would interfere with achieving this goal because of: (1) the decrease in the incentive to conserve electricity that occurs as the price signal that customers receive for each additional unit of usage (kWh) is diminished when cost recovery is shifted from the rate per kWh to the customer charge and (2) the decreased energy efficiency program participation rates that will occur as payback periods for customer energy efficiency investments are increased by shifting cost recovery from rates per kWh to fixed residential customer charges that do not vary based on usage or demand. (Exhibit 401, Kind Surrebuttal Testimony, page 3)

Public Counsel opposes Ameren Missouri's proposal to raise the customer charges because the cost study on which that proposal is based is not reliable, in that the Company classified too much energy- or demand-related cost as customer-related in its calculation of customer charge levels. Ameren Missouri used the zero intercept method to classify distribution system costs as customer-related or demand-related. This method attempts to mathematically derive the hypothetical cost of a hypothetical distribution system built serve customers that use no electricity, a distribution system that does not actually need to distribute electricity. This approach is fraught with errors from a conceptual standpoint, and an examination of the Company's analysis quickly reveals that it has produced absurd results.

Ameren Missouri witness William Warwick described Exhibit 410 as a listing of the accounts containing all of the distribution system plant, from the substation fence all the way to the service drop. (Transcript, page 2069) Exhibit 410 shows that, according to the Company's zero-intercept analysis, the conduits in a system built to deliver no electricity would cost almost 70% of the cost of today's actual system – built to deliver lots of electricity. The cables (the actual electricity-conducting copper or aluminum cable) in this hypothetical no-load system

would also cost 70% of the cost of the actual system. In the hypothetical system that does not need to deliver any electricity, Ameren Missouri's analysis shows that transformers would cost 57% of the cost of transformers in the real system. While these percentages are obviously and ridiculously high, Ameren Missouri's analysis showed that only 40% of the cost of overhead services would be needed in the hypothetical zero-load system. This figure is obviously and ridiculously low; a service drop is needed to connect every customer to the system, and many customers on the real-world system have service drops of the minimum size actually installed. The numbers just do not make any sense and the Commission should not rely on them to increase customer charges in this case.

The end result of the Company's zero-intercept analysis is that the Company classified a much greater amount of distribution system costs as customer-related than did either the Staff or Public Counsel. Staff witness Michael Scheperle did not include any amounts from accounts 364 through 368 in his calculations of appropriate customer charges. (Transcript, pages 2147-2148) He conceded that he had done so in the past, but has reconsidered and no longer considers it appropriate.

Public Counsel also opposes Staff's proposal to raise customer charges for residential and small general service customers. Staff proposes to raise the residential customer charge from \$8.00 to \$9.00, and to raise the small general service customer charges by the same percentage as the overall increase awarded by the Commission in this case. Staff bases this proposal on its cost study, which indicates that the highest cost-based customer charge for residential customers would be \$8.97. (Transcript, pages 2148-2149) The biggest problem with Staff's proposed increase is that Mr. Scheperle included uncollectibles, or bad debts, in his calculation of customer-related costs. But Mr. Scheperle conceded that the bad debt amount is more energy-

related than customer-related. (Transcript, page 2149) While the precise effect of Staff's inclusion of the energy-related portion of bad debts as customer-related is not calculated in the record, it would reduce the customer-related costs in Staff's study, which only supports an $8.97 customer charge even with the erroneous inclusion.

Ameren Missouri, primarily through the testimonies of its witness William Davis, presented evidence that allegedly shows the impact of the proposed customer charge increase on low-income customers. But there are so many flaws in that analysis that the Commission cannot rely on it. The Company never performed any studies regarding energy usage based on household income or based on the percentage of household income that goes to pay for energy. (Transcript, pages 2081-2082) And with respect to its proposal, Ameren Missouri does not know either the number of customers or the percent of customers that would see an above average increase as a result of the proposed customer charge increase. (Transcript, page 2097) In effect, the Commission would be shooting blind if it allowed the Company to implement its proposed increase, without knowing how many customers would be more adversely affected.

Despite Ameren Missouri's attempts to deny or minimize the effect, the record is clear that its proposal would have a chilling effect on energy efficiency. Ameren Missouri admits as much when pressed. (Transcript, pages 2115-2118) Its proposal would shorten the payback period for customers by 1.7%. (Transcript, page 2110) While that is not a huge amount, it is considerably larger than the benefits to LIHEAP participants that Mr. Davis points out in his rebuttal testimony at page 12 (Exhibit 39). That percentage is just a few tenths of a percent, but Ameren Missouri considered it worth noting in the prefiled testimony. (Transcript, pages 2131-2132)

Similarly, while Ameren Missouri criticizes NRDC witness Morgan for failing to perform

a quantitative analysis and only presenting a directional analysis, it did exactly the same thing. Mr. Davis testified in his rebuttal testimony (Exhibit 39, page 16) that Ameren Missouri's proposed increase customer charge could have a beneficial impact in a hot summer. But Mr. Davis did not do a quantitative analysis to quantify how much of a benefit the proposal might confer in a hot summer. Mr. Davis conceded that this analysis was merely a directional one (Transcript, page 2132) like the directional analysis that he criticizes Ms. Morgan for performing.

And Ameren Missouri did not do any analysis whatsoever to determine whether its customers who received LIHEAP are representative of its low income customers in general. (Transcript, page 2127) Although Ameren Missouri witness Davis tried to equate the use of LIHEAP customers to the sample of customers chosen for load research data, he quickly admitted that the customers in the load research sample are specifically chosen to comprise a representative sample. (Transcript, page 2128) He also admitted that the LIHEAP customer group was not. (Transcript, page 2128)

In fact, there has been no thorough investigation in this case into the effect of increasing the customer charge on low-income customers. (Transcript, page 2150) That fact – on top of all the reasons set forth above – should cause the Commission grave concern about raising the customer charges in this case.

WHEREFORE, Public Counsel respectfully offers this Initial Post-hearing Brief and prays that the Commission conform its decision in this case to the arguments contained herein.

Respectfully submitted,

OFFICE OF THE Public Counsel

/s/ Lewis R. Mills, Jr.

By:______________________________
Lewis R. Mills, Jr. (#35275)
Public Counsel
P O Box 2230
Jefferson City, MO 65102
(573) 751-1304
(573) 751-5562 FAX
lewis.mills@ded.mo.gov

CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing have been emailed to all parties this 5th day of November 2012.