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

COMMENTS OF STAFF COUNSEL

On November 7, 1995, Union Electric Company (UE) petitioned the Missouri Public Service Commission (MoPSC or Commission) for approval of the proposed merger of UE and CIPSCO Incorporated (CIPSCO), the parent company of Central Illinois Public Service Company (CIPS). In its application, UE proposes a holding company structure where Ameren Corporation (Ameren) will own all of UE's and CIPSCO's stock and become a registered public utility holding company under the Public Utility Holding Company Act of 1935 (PUHCA).[1] Due to the legal issues raised by the form of the proposed merger, i.e., regulating a public utility company which is owned by a registered holding company, the Staff of the Commission believes that filing these comments with the Staff testimony is the most effective way to bring its legal concerns to the Commission. Although the Staff intends to brief these matters based upon the record established in this case, the Staff believes that it would be prudent to note these items before the hearing so the Commission has the opportunity to ensure that a complete record is developed to its satisfaction.

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[1] 15 U.S.C. § 79. et. seq.

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I. The Commission must address the impact of the merger on its ability to regulate UE.

Under Missouri law the Commission must approve the proposed merger unless it is detrimental to the public interest.[2] One of the factors the Commission may consider when determining if this standard is met is whether effective MoPSC regulation will be impaired or diminished by the merger.

The MoPSC itself has raised the loss of jurisdiction question in the UE/CIPSCO merger proceeding at the Federal Energy Regulatory Commission (FERC).[3] In response, UE argued that this issue does not belong at FERC since the MoPSC has the opportunity to address the loss of jurisdiction during the merger approval process at the state level.[4] The instant comments focus on the jurisdictional issues which the MoPSC must address in this case.

II. The proposed merger will fundamentally alter UE's corporate structure in that many of UE's current functions may be performed by Ameren subsidiaries, which would be regulated by the Securities and Exchange Commission under PUHCA.

UE is currently organized as a holding company. UE is exempt from registration under Section 3 of PUHCA because it meets the statute's integration requirement. Since registration is not

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2 See, State ex rel. City of St. Louis v. Public Service Comm., 73 S.W. 2d 393 (Mo. banc 1934); State ex rel. Fee Fee Trunk Sewer, Inc. v. Litz, 596 S.W. 2d 466 (Mo. App. 1980).

3 Notice of Intervention, Request for Hearing and Motion to Consolidate, FERC Docket Nos. EC-96-7-000 and ER-96-679-000, pp. 8-11.

4 Answer of Applicants to Motions and Requests for Hearing, FERC Docket Nos. EC-96-7-000 and ER96-679-000, p. 37.

required, UE is not currently subject to most PUHCA regulation. CIPSCO is also an exempt holding company. Under the terms of the proposed merger, UE and CIPSCO will merge to form Ameren.

Ameren will not meet the integration requirements of PUHCA and will have to register with the Securities and Exchange Commission (SEC) and be subject to extensive PUHCA regulation. Ameren is a Missouri corporation and will have two wholly owned operating utility subsidiaries, UE and CIPS. In addition, Ameren could form any number of subsidiaries or affiliates, including nonutility businesses.

One subsidiary that is already formed is Ameren Services Company (Ameren Services). Ameren Services is a utility services company which will be regulated by the SEC under section 13 of PUHCA. Ameren Services will perform the functions that are now performed by UE such as plant maintenance and fuel purchasing.

UE maintains in its response to Staff Data Request No. 113 and 185 that Ameren Services will not be regulated by the MoPSC. Thus, after the merger, some of UE's utility operations will be carried out by an entity which, according to UE, will not be regulated by the MoPSC. UE has not specified what the exact nature of the services which Ameren Services will provide to UE, although PUHCA contains no restrictions on what services Ameren Services can perform for UE as long as the transactions meet SEC scrutiny.

UE's choice of the registered holding company structure dramatically changes the operation of UE. The potential exists for Ameren Services to perform most of the activities currently carried out by UE. The registered holding company structure will necessarily increase the number of transactions UE has with affiliated companies. The MoPSC must ensure that it has the ability to

access information concerning these transactions and make adjustments in UE's rates for transactions which are deemed to be unjust, unreasonable, imprudent, and/or otherwise adverse to ratepayers.

III. The potential impact of PUHCA on MoPSC regulation.

The registered holding company structure chosen by UE may impact MoPSC regulation of UE's transactions with affiliates. Transactions between Ameren Services and UE are unlawful under section 13(b) of PUHCA, unless they are approved by the SEC. The SEC has established affiliate transaction rules which restrict the pricing of goods and services among affiliated companies of a registered holding company to cost as defined by the rules.[5] The jurisdiction of the SEC over UE's affiliate transactions could preempt MoPSC jurisdiction. At the wholesale level, the Ohio Power Company,[6] an operating utility affiliate of a registered holding company, has successfully argued that the SEC alone has jurisdiction over the price affiliated companies may charge each other for goods.

a. Overview of the preemption problem.

In Ohio Power Co. v. FERC, the U. S. Court of Appeals for the D.C. Circuit held that SEC approval of a sale of coal from a nonutility affiliate to a utility affiliate of a registered holding company required the FERC to defer to the SEC determined price when setting rates. The Court based its decision on two independent grounds. First, FERC's disallowance was contrary to one of its own regulations which stated that any fuel purchases that are subject to price regulation by a regulatory body are deemed reasonable. More importantly, the Court held that the SEC's specific

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5 17 CFR § 250.90, 91, 92.

6 Ohio Power Co. v. FERC, 954 F. 2d 779 (D.C. Cir. 1992), cert. denied, 113 U.S. 483 (1992).

statutory mandate to establish a cost-based price for sales of goods between holding company affiliates constrained FERC from altering that price under its "just and reasonable" rate setting authority.

When one regulating entity disallows costs which are approved by another regulatory entity, those costs are described as "trapped". The Court held that FERC could not set a rate which trapped SEC determined costs.[7] Should the MoPSC disagree with the SEC determined price for goods or services purchased by UE from an affiliate, the Ohio Power decision may provide an opportunity for UE to argue that the Commission cannot establish a rate which traps these costs.

This potential loss of state jurisdiction must be addressed by the Commission in this proceeding. State commissioners from two states have testified before Congress that the trapped costs rationale of Ohio Power may prevent effective state rate regulation of electric utilities of non-exempt holding companies.[8]

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[7] Id. at 786.

[8] See, Proposals to Allow Entry of Registered Utility Holding Companies to Provide Telecommunication Services: Hearings Before the Subcomm. on Energy and Power of the House Comm. on Energy and Commerce, 103rd Cong. 2d Sess. (1994) (prepared statement of Commissioner Ronald E. Russell of the Michigan Public Service Commission on behalf of the National Association of Regulatory Utility Commissioners); Registered Holding Company Transactions: Hearings Before the Subcomm. on Energy and Power of the House Comm. on Energy and Commerce, 103rd Cong. 2d. Sess. (1994) 86-89 (prepared statement of Craig A. Glazer, Chairman of the Public Utilities Commission of Ohio on behalf of the National Association of Regulatory Utility Commissioners).

In response to Staff Data Request No. 144, UE agreed that an Ohio Power type argument could be made in which the MoPSC is precluded from questioning the cost or revenue levels incurred by UE under SEC jurisdictional agreements. UE also stated in its response that it does not intend to make such an argument.

b. The Commission should preserve its jurisdiction over affiliate transactions.

While the impact of the Ohio Power decision on MoPSC jurisdiction is not certain, the Commission must make certain that the proposed merger does not adversely impact its jurisdiction. Simply deferring this issue in the face of a possibility that the Commission's authority is preempted by the SEC is detrimental to the public interest since the MoPSC is capable of, has the expertise for, and is charged under Missouri law with making decisions respecting safe and adequate utility service and just and reasonable rates. Also, should the Commission defer this issue and approve the merger without any safeguards, it may be precluded from addressing this issue at a later time.

UE must commit that it will not claim that SEC review of affiliate agreements under PUHCA in any way displaces this Commission's review of UE's affiliate agreements.[9] The Commission may also want to explore the option of approving UE's affiliate transactions before SEC approval.[10]

Since UE has not filed the services agreement between Ameren Services and UE with the MoPSC, the Staff has not had an opportunity to determine if the services agreement negatively impacts Missouri ratepayers. Review of the superseded general services agreement filed on November 7, 1995 is no substitute for review of the UE/Ameren Services service agreement. The

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9 This condition is No. 1 on Attachment 1 to these comments.

10 This condition is No. 2 on Attachment 1 to these comments.

Commission should not approve the merger until it has had the opportunity to review and consider approval of the yet to be filed services agreement.

Assuming UE makes the required commitments to ensure effective state regulation, the Commission's approval of the merger should be conditioned on FERC and SEC approval of UE's commitments to the MoPSC. In this way, the MoPSC sanctioned conditions become part of the agreements reached at the federal level and make compliance with the MoPSC conditions necessary for the effectiveness of UE's and Ameren's SEC and FERC filings.

IV. The Commission should examine the effect of FERC jurisdiction over electric energy transactions between UE and CIPS.

Under the proposed merger, UE and CIPS will provide electric energy to each other under a Joint Dispatch Agreement (JDA) and a System Support Agreement (SSA). The JDA allows for the coordinated operation of UE's and CIPS' generation and transmission resources and allocates the benefits and costs of coordinated operation. The SSA is a contract whereby UE will provide capacity and energy to CIPS to serve UE's former Illinois customers if they are transferred to CIPS. Although the JDA and SSA will be filed at FERC and are subject to FERC jurisdiction, UE is asking for Commission authorization to enter into and perform the JDA and SSA.

While under Ohio Power the SEC has jurisdiction over the pricing of transactions among affiliates of a registered holding company, that decision did not involve the sale of electric energy among affiliates. The contracts for the sale of electricity between holding company affiliates are subject to the jurisdiction of FERC. Section 2 of PUHCA defines "sales contract" to exclude the sale of electric energy or natural or manufactured gas. The SEC's jurisdiction under PUHCA

does not extend to the sale of electric energy among subsidiaries of a registered holding company.[11]

FERC has jurisdiction over wholesale electric energy transactions. A state utility commission must allow, as reasonable operating expenses, costs incurred by a utility as a result of paying a FERC-determined wholesale rate.[12] FERC approval of an energy supplier's rate does not necessarily mean it was reasonable for the purchaser to incur the expense. A state commission can challenge the prudence of a utility's decision to purchase power at a FERC approved rate under what has come to be known as the Pike County doctrine.[13] The MoPSC, in the context of a gas case, has recognized the Pike County doctrine[14] and there appears to be authority for applying the Pike County doctrine in the natural gas utility context.[15]

A state commission must also defer to certain FERC approved allocations contained in operating or system agreements among affiliates of a registered holding company.[16] These

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11 See, Mississippi Industries v. FERC, 808 F. 2d 1525, 1550 (D.C. Cir., 1987), cert. denied sub nom, Arkansas Public Service Commission v. FERC, 484 U.S. 985 (1987); Cincinnati Gas & Electric Company and PSI Energy, Inc., 64 FERC ¶61.237.

12 See, Nantahala Power and Light Co.v. Thornburg, 476 U.S. 953 (1986).

13 See, Pike County Light and Power Co. v. Pennsylvania Public Utility Commission, 465 Ad. 2d. 735 (Pa. 1983).

14 American National Can Company v. Laclede Gas Company, 30 Mo.P.S.C. (N.S) 32, 35 (1989).

15 Kentucky West Virginia Gas Co. v. Pennsylvania Public Utility Commission, 837 F. 2d 600 (3rd Cer. 1988), cert. denied, 488 U.S. 941 (1988).

16 Mississippi Power & Light Co. v. Miss. Ex. Rel. Moore, 487 U.S. 354 (1988).

allocations between affiliates affect wholesale electric energy power rates which must be passed through to retail customers.

a. Under a holding company structure, electric energy transactions between affiliated companies are FERC jurisdictional.

Under the proposed merger, UE and CIPS are separate operating companies. Electric energy transactions between the two companies are subject to FERC jurisdiction. These transactions, which, among other things, include the allocation of off system sales and transmission revenues, are the subject of the JDA and the SSA.

Had UE chosen a unitary structure, where one company operated in both states through operating divisions, there would be no wholesale transactions occurring between operating companies and no FERC jurisdiction. Both the Illinois and Missouri Commissions would clearly have jurisdiction to determine the reasonableness of the JDA and the SSA under a unitary structure. The JDA contains general allocation principals which apply to UE and CIPS. Because of the lack of specifics, the Staff, although comfortable with the general concept of the JDA, cannot determine if the JDA negatively impacts Missouri ratepayers. For more information concerning the JDA and SSA, see the testimony of Staff witness Dan Beck.

In its FERC intervention filing, this Commission raised the issue that it may be forced to set retail rates which reflect the costs incurred or revenues received under the FERC-jurisdictional JDA and SSA.[17] After the merger, if the MoPSC believes that an allocation under the JDA is not fair to Missouri ratepayers and attempts to make an adjustment, UE could argue that the MoPSC may

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[17] Notice of Intervention, Request for Hearing and Motion to Consolidate, p. 8.

not alter the FERC ordered allocation. In addition, if this Commission authorizes UE to enter into the JDA as part of this Commission's approval of the merger, it may be contended that this Commission may not make a prudence challenge under the Pike County doctrine. It should be noted that the MoPSC in its FERC intervention filing in the UE/CIPSCO merger proceeding seeks to distinguish the instant situation from the Mississippi Power & Light case. The MoPSC in its FERC intervention filing states that the instant case is different than Mississippi Power & Light because (1) the costs to be shared under the proposed JDA and SSA agreements are not the product of joint planning by UE and CIPSCO, (2) UE's decision to enter into these agreements, and the matters relating to the costs incurred and the revenues received thereby, is voluntary, i.e., none of these matters is the result of a FERC order, and (3) the retail rate treatment of future costs under these agreements are subject to conditions that may be imposed by this Commission in the instant proceeding.[18]

b. The Commission should ensure its jurisdiction over the transactions contained in the Joint Dispatch Agreement and System Support Agreement.

The Commission must be permitted to allow or deny recovery of and determine the prudence or imprudence of JDA and SSA costs and other allocations sought to be recovered in retail rates by UE as well as to determine the details of the derivations of charges and allocations, such as projections, estimates, accounting determinations, made under the JDA and SSA.[19]

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[18] Id. at 9.

[19] This condition is No.3 on Attachment 1 to these comments.

The JDA and SSA also permit changes to said agreements for any reason. Thus, even if the Commission is comfortable with the JDA and SSA and the effect on Missouri ratepayers, there is no guarantee that the JDA or SSA will not be changed. The Commission should reserve the right to approve changes to the JDA and SSA as a condition of its approval of the merger. As with the PUHCA conditions, the Commission should condition its approval of the merger on FERC approval of the MoPSC conditions.

V. The effect of the merger on the Commission's ability to regulate UE's gas operations is uncertain.

UE has provided very few details on how the merger will effect its gas operations. UE has not provided any details of how UE and CIPS will jointly operate their gas facilities. If an operating agreement is filed between UE and CIPS regarding joint operation of gas facilities, and other matters, the question of FERC jurisdiction over this agreement will occur. The Commission must protect its jurisdiction in this area no less than in the electric area.[20] The rebuttal testimony of Michael J. Wallis addresses these matters.

VI. Conclusion

The above comments demonstrate that the proposed merger raises questions about the ability of the Commission to regulate UE after the merger. UE should not expect approval of a merger which does not preserve the effectiveness of MoPSC regulation. In order for the Commission to approve the merger, UE must commit in this proceeding, and in proceedings before the SEC and FERC, to maintain MoPSC jurisdiction.

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[20] This condition is No. 4 on Attachment 1 to these comments.

Respectfully Submitted,

Roger W. Steiner
Assistant General Counsel
Missouri Bar #39586
573/751-7434

Aisha Ginwalla
Assistant General Counsel
Missouri Bar #41608
573/751-6726

Steven Dottheim
Deputy General Counsel
Missouri Bar #29149
573/751-7433

Attorneys for the Staff of the
Missouri Public Service Commission
P. O. Box 360
Jefferson City, MO 65102
573-751-9285 (Fax)

CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing have been mailed or hand-delivered to all counsel of record as shown on the attached service list this 7th day of May, 1996.

ATTACHMENT 1

1. All contracts, agreements, or arrangements of any kind, required to be filed with and/or approved by the Securities and Exchange Commission (SEC) pursuant to the Public Utility Holding Company Act of 1935 as subsequently amended, between the Union Electric Company (UE), and any affiliate, associate, holding, mutual service, or subsidiary company, within the same holding company system, as these terms are defined in 15 U.S.C. §79b as subsequently amended, shall contain and be conditioned upon the following without modification or alteration: UE and Ameren Corporation will not seek to overturn, reverse, set aside, change or enjoin, whether through appeal or the initiation or maintenance of any action in any forum, a decision or order of the Missouri Public Service Commission (MoPSC) which pertains to recovery, disallowance, deferral, or ratemaking treatment of any expense, charge, cost, or allocation incurred or accrued by UE 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 SEC, or was incurred pursuant to a contract, arrangement, agreement, or allocation method which was filed with or approved by the SEC. Failure to include the above language in any such contract, agreement, or arrangement shall render the same voidable at the sole discretion of the MoPSC. Should the above language be altered or invalidated by any Court or governmental agency, such contract, agreement, or arrangement shall be voidable at the sole discretion of MoPSC.

2. Any Affiliate Contract which needs to be filed with the SEC will first be filed with the Missouri Public Service Commission (MoPSC) for approval. Should the MoPSC reject the Affiliate Contract, UE will withdraw its filing at the SEC. If the Affiliate Contract has been approved by the SEC, UE will terminate the contract pursuant to its terms.

Affiliate Contract is defined as a contract, or any amendment to an Affiliate Contract, between UE and any affiliate, associate, holding, mutual service, or subsidiary company, within the same holding company system, as these terms are defined in 15 U.S.C. §79b as subsequently amended, providing for:

(i) the operation of any part of UE's generating, transmission and/or distribution facilities by an affiliate;

(ii) the purchase or sale of assets, goods or services to or from an affiliate; and

(iii) the assumption by UE of any liability as a guarantor, endorser, surety, or otherwise is respect of any security or contract of an affiliate.

3. All wholesale electric energy or transmission service contracts, agreements, or arrangements of any kind, including the Joint Dispatch Agreement respecting Union Electric Company (UE) and any Ameren Corporation subsidiary or affiliate required to be filed with and/or approved by the

Federal Energy Regulatory Commission (FERC) shall contain and be conditioned upon the following without modification or alteration: UE and Ameren Corporation will not seek to overturn, reverse, set aside, change or enjoin, whether through appeal or the initiation or maintenance of any action in any forum, a decision or order of the Missouri Public Service Commission (MoPSC) which pertains to recovery, disallowance, deferral, or ratemaking treatment of any expense, charge, cost, or allocation incurred or accrued by UE in or as a result of a wholesale electric energy or transmission service contract, agreement, arrangement, or transaction, on the basis that such expense, charge, cost, or allocation has itself been filed with or approved by the FERC, or was incurred pursuant to a contract, arrangement, agreement, or allocation method which was filed with or approved by the FERC. Failure to include the above language in any such contract, agreement, or arrangement shall render the same voidable at the sole discretion of the MoPSC. Should the above language be altered or invalidated by any Court or governmental agency, such contract, agreement, or arrangement shall be voidable at the sole discretion of MoPSC.

4. All gas supply, storage, and/or transportation service contracts, agreements, or arrangements of any kind respecting Union Electric Company (UE) and any Ameren Corporation subsidiary or affiliate required to be filed with and/or approved by the Federal Energy Regulatory commission (FERC) shall contain and be conditioned upon the following without modification or alteration: UE and Ameren Corporation will not seek to overturn, reverse, set aside, change or enjoin, whether through appeal or the initiation or maintenance of any action in any forum, a decision or order of the Missouri Public Service Commission (MoPSC) which pertains to recovery, disallowance, deferral, or ratemaking treatment of any expense, charge, cost or allocation incurred or accrued by UE in or as a result of a gas supply, storage, and/or transportation service contract, agreement, arrangement, or transaction, on the basis that such expense, charge, cost, or allocation has itself been filed with or approved by the FERC, or was incurred pursuant to a contract, arrangement, agreement, or allocation method which was filed with or approved by the FERC. Failure to include the above language in any such contract, agreement, or arrangement shall render the same voidable at the sole discretion of the MoPSC. Should the above language be altered or invalidated by any Court or governmental agency, such contract, agreement, or arrangement shall be voidable at the sole discretion of the MoPSC.