BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

The Staff of the Missouri Public Service Commission, Complainant, vs. Union Electric Company, Respondent.	)	CASE NO. EC-87-114
Douglas M. Brooks, Public Counsel for the State of Missouri, Complainant, vs. Union Electric Company, Respondent.	)	CASE NO. EC-87-115

APPEARANCES: Paul A. Agathen, and James J. Cook, Attorneys at Law, P. O. Box 149, St. Louis, Missouri 63166, for Union Electric Company.

William M. Barvick, Attorney at Law, 231 Madison Street, Jefferson City, Missouri 65101, for International Brotherhood of Electrical Workers, Local 1439, International Brotherhood of Electrical Workers, Local 1455 and International Union of Operating Engineers, Local 148.

Gerald T. McNeive, Jr., Associate General Counsel, 720 Olive Street, Room 1528, St. Louis, Missouri 63101, for Laclede Gas Company.

Stephen J. Cassin, Robert C. Johnson, and George M. Pond, Attorneys at Law, Peper, Martin, Jensen, Maichel and Hetlage, 720 Olive Street, 24th Floor, St. Louis, Missouri 63101, for Monsanto Company, et al.

William C. Kelly, Assistant Attorney General, P. O. Box 899, Jefferson City, Missouri 65102, for the State of Missouri.

Willard C. Reine, Attorney at Law, 314 East High Street, Jefferson City, Missouri 65101, for Missouri Retailers Association.

Richard W. French, First Assistant Public Counsel, P. O. Box 7800, Jefferson City, Missouri 65102, for the Office of the Public Counsel and the Public.

William C. Harrelson, General Counsel, Paul H. Gardner, Deputy General Counsel, Thomas M. Byrne, and Cecil I. Wright, Assistants General Counsel, P. O. Box 360, Jefferson City, Missouri 65102, for the Staff of the Missouri Public Service Commission.

HEARING EXAMINER: Martha S. Hogerty

UNION ELECTRIC COMPANY

Case Nos. EC-87-114 and EC-87-115

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REPORT AND ORDER
PROCEDURAL HISTORY

On April 9, 1987, the Commission issued its Order delegating to its Staff authority to prosecute a complaint as to the reasonableness of the rates and charges of Union Electric Company (hereinafter referred to as UE or Company).

On April 24, 1987, the Staff filed a complaint against UE alleging that its current rates are excessive and should be reduced. The Staff requested the Commission to establish proceedings to determine and fix rates which are just and reasonable. Concurrent with the filing of the complaint, Staff filed its prepared direct testimony and its "Motion To Limit The Scope Of The Proceedings, Establish A Procedural Schedule, Schedule An Early Hearing On Phase-In Accruals And Issue An Order Making Phase-In Accruals Interim Subject To Adjustment" and suggestions in support thereof.

On April 29, 1987, the Commission issued an order directing UE to file its answer to the complaint on or before May 26, 1987 and setting an intervention deadline for May 26, 1987.

On April 30, 1987, the Office of the Public Counsel for the State of Missouri (hereinafter Public Counsel) filed a complaint against UE alleging that its current rates are excessive and are not just and reasonable. The Public Counsel requested the Commission to institute proceedings to determine just and reasonable rates. Concurrent with the filing of the complaint, Public Counsel filed its "Motion To Consolidate Cases" requesting the Commission to consolidate Case No. EC-87-115 with the pending complaint case filed by the Staff (Case No. EC-87-114).

On May 6, 1987, the Commission issued its order directing UE to file its answer to the complaint on or before June 1, 1987, and setting an intervention deadline in Case No. EC-87-115 for June 1, 1987.

On May 26, 1987, UE filed its answer and motion to dismiss Case No. EC-87-114 and on May 29, 1987, UE filed its answer and motion to dismiss Case No. EC-87-115. The answers generally deny the allegations complained of.

By order issued June 22, 1987, the Commission denied UE's motion to dismiss, consolidated Case Nos. EC-87-114 and EC-87-115 and set a procedural schedule. The order denied Staff's request to schedule an interim hearing to address whether phase-in accruals should be made interim, subject to refund. The Commission granted Staff's motion to limit the scope of the hearing and limited the scope of the proceeding to issues related to the Company's revenue requirement and methods of allocating any change in revenue requirement among the various classes to maintain the existing rate design.

In the same order, the Commission granted intervention to the following parties: Missouri Retailers Association, the State of Missouri, Anheuser-Busch, Inc., Monsanto Company, American National Can Company, Chrysler Corporation, Continental Cement Company, Dundee Cement Company, Emerson Electric Company, Ford Motor Company, General Motors Corporation, Mallinckrodt, Inc., McDonnell Douglas Corporation, and PPG Industries, Inc. (Monsanto, et al), the City of Cape Girardeau, Laclede Gas Company, Local 1455 of the International Brotherhood of Electrical Workers (IBEW 1455), Local 1439 of the International Brotherhood of Electrical Workers (IBEW 1439), Local 148 of the International Union of Operating Engineers (IUOE 148), the Doe Run Company, Nooter Corporation, Pea Ridge Iron Ore Company, River Cement Company, Gerald A. Rimmel, Receiver, Mansion House Center Properties (Mansion House), the Metropolitan St. Louis Sewer District, the City of Old Monroe, the City of Moberly, and the Missouri Public Interest Research Group (MoPIRG).

Pursuant to the Commission's June 22, 1987 order as modified by a subsequent order issued August 21, 1987, a prehearing conference was conducted at the Company's offices. The following parties participated in the prehearing conference: the Staff, the Company, the Public Counsel, Monsanto, et al., Laclede Gas Company,

the Missouri Public Interest Research Group, IUOE 148, IBEW 1455, IBEW 1439, the State of Missouri and Missouri Retailers Association.

Hearings were held in this proceeding commencing September 14, 1987, continuing from day to day through September 25, 1987.

Pursuant to the briefing schedule subsequently established by the Hearing Examiner, initial briefs were filed on October 29, 1987, by the Company, the Public Counsel, the Staff, Laclede Gas Company and Monsanto, et al. On November 19, 1987, reply briefs were filed by the Company, the Public Counsel, the Staff, and Monsanto, et al.

During the course of the Commission's deliberations, the parties were requested to calculate reconciliations based upon various assumptions resolving the issues in this case. The requests and the parties' responses have been marked as late-filed exhibits and received into the record.

Findings Of Fact

The Missouri Public Service Commission, having considered all of the competent and substantial evidence upon the whole record, makes the following findings of fact:

I. Test Year - True-Up

Staff uses a test year based on calendar year 1986. The Staff makes only two contested adjustments to the test year, an adjustment to the capital structure and the use of 1987 billed franchise taxes. These adjustments are discussed in Section IV. B. and V. A. set forth below.

UE proposes various adjustments to the 1986 test year. All of the Company's adjustments increase revenue requirement and most are based upon partially budgeted or forecasted data. Since the purpose of a test year is to match revenue, expenses and rate base for the purpose of setting rates for the future, it is inappropriate to make isolated adjustments to the test year. Such adjustments tend to distort the proper matching of revenue, expense and rate base.

The evidence shows that the Company's earnings trend is positive. Its revenues are increasing, its fuel costs are decreasing and its rate base is declining. Information reflecting the first six months of 1987 suggests that several categories of expenses are declining and overall it appears that the Company's cost of service is declining. In the Commission's opinion, it would be inappropriate to make isolated adjustments beyond the test year which would recognize certain categories of increased expenses without recognizing those that are decreasing. Since the evidence does not point to a cost of service increase subsequent to the 1986 test year, adjustments outside the 1986 test year shall not be allowed for purposes of this case, absent a strong justification.

By motion filed July 30, 1987, the Company filed its request to true-up the following items to December 30, 1987: (1) the accumulated phase-in credit balance; (2) unprotected excess deferred taxes; (3) Westinghouse credits; (4) accumulated deferred taxes; (5) distribution of clearing accounts during 1986. During the course of the hearing the Company requested the Commission to true-up the capital structure at September 30, 1987. Finally, by motion filed November 25, 1987, the Company petitioned the Commission to reopen proceedings for the purpose of introducing additional evidence respecting 1987 wage and benefit increases.

The Commission determines that the accumulated phase-in credit balance at December 31, 1987, shall be used for purposes of this case and, therefore, the Company's motion is granted with respect to the updating of this item. Although the inclusion of this item reflects an adjustment one year beyond the test year, it must be included for reasons unrelated to the matching principle. This item is unique as it reflects revenue requirement deferred under the phase-in plan adopted by this Commission in Case Nos. EO-85-17 and ER-85-160, Re: Union Electric Company, 66 P.U.R.4th 202, 27 Mo. P.S.C. (N.S.) 183 (1985) (hereinafter the Callaway rate case). As is discussed below, the previously approved phase-in plan is being modified in this Report and Order and the accruals shall end as of December 31, 1987. Since

these accruals represent costs deferred under the phase-in plan which the Company is entitled to receive, it is proper to include these amounts in the calculation of phase-in credits to be amortized over a five year period as discussed below. Thus, the Company is assured of recovery of all deferred costs which have arisen out of the phase-in plan established by this Commission.

For the same reasons set out above regarding the use of a 1986 test year, the Commission concludes that no other item shall be trued up as the Company's true-up request focuses on items which increase revenue requirement while ignoring other factors which would tend to decrease revenue requirement.

Company's earnings have been shown to be excessive. In this case its current return on equity is being adjusted downward from 15.62 percent to 12.01 percent. Essentially, it is only because of the need to recover the phase-in accruals that any increase is warranted beyond the current phase-in year. Thus, to reflect only items that tend to increase revenue requirement without reflecting items tending to decrease revenue requirement will not result in rates that are fair, just, and reasonable. Accordingly, the Commission determines that any adjustment beyond the test year shall not be used in this case, unless a persuasive reason is advanced in its favor.

II. Rate Base Issues

A. Callaway I Disallowed Costs

Staff proposes to reduce net plant in service to reflect disallowed Callaway plant based on the current allocation factor. Company opposes Staff's adjustment on the ground that the disallowed portion of Callaway should be reflected at the same dollar amount as reflected in the Callaway rate case.

The Commission disallowed $384 million from the Missouri jurisdictional portion of Callaway in the Callaway I rate case. In that case, the Missouri allocation factor for production cost was 80.70 percent while in the instant case the allocation factor is 84.33 percent. Thus, a greater portion of the Callaway plant

will be allocated to Missouri in the instant case than was allocated in the Callaway rate case. Staff proposes to factor up the $384 million in disallowed costs to correspond to the increased level of total Missouri jurisdictional costs. Staff contends this approach is reasonable and is consistent with paragraph 5 of the Stipulation and Agreement which settled the Callaway I rate case appeal between Company, Staff and Public Counsel. As part of that settlement, Company agreed not to seek inclusion in future cases of any disallowed costs and Staff and Public Counsel agreed not to seek any further disallowances. The last paragraph of the Stipulation and Agreement provides that:

> This Stipulation and Agreement does not apply to additional recovery or disallowance of Callaway costs on the basis of proposed changes in jurisdictional allocation factors.

Although Staff's approach is not inconsistent with the Stipulation and Agreement discussed above, the Commission deems it inappropriate to change the disallowed portion of Callaway plant as a result of a change in jurisdictional factors. This approach could result in a portion of the Callaway plant not being recovered by the Company if each jurisdiction does not adjust the disallowed plant during each rate proceeding. It is unknown whether another jurisdiction would be willing to decrease the amount of disallowed plant if the jurisdictional factor decreases.

In addition, the $384 million amount which the Commission disallowed included a $100 million rate base disallowance which was not calculated on a total Company basis and then allocated to Missouri based on the 80.7 percent allocation factor. Thus, the effect of Staff's adjustment is to increase the disallowance applicable to Missouri above that which was disallowed in the Callaway I rate case.

Based on the foregoing, the Commission finds that the Staff's adjustment should be rejected.

B. Callaway I Unreviewed Costs

Staff has included in rate base $113 million on a Missouri jurisdictional basis related to Callaway construction costs which were not reviewed in the Callaway rate case.

Public Counsel excludes Callaway I unreviewed costs on the ground that the costs are unique and, therefore, the Company has the burden of producing evidence which would justify the inclusion of these costs. In support of its argument, Public Counsel cites Section 393.512(2), RSMo 1986 which states in pertinent part as follows:

> ...At any hearing involving a rate sought to be increased, the burden of proof to show that the increased rate or proposed increased rate is just and reasonable shall be upon the...electrical corporation...

In the Commission's opinion Public Counsel's reliance on this statutory section is misplaced as it refers to rate cases initiated by the Company. There is no dispute that these costs are associated with the Callaway Plant which, absent a finding of unreasonableness or imprudence, should be properly included in rate base. Public Counsel and the Staff initiated these complaint cases and, therefore, if an issue is to be made of a particular cost or plant item it is incumbent upon the Complainants to audit these costs to determine their reasonableness. If Public Counsel's position were to be accepted, these costs could be kept out of rate base indefinitely by Staff's and Public Counsel's decision not to audit.

Public Counsel suggests two alternatives to total nonrecognition of these costs: (1) The Commission could estimate the amount to be disallowed by applying the percentage of disallowances made by the Commission in the Callaway rate case to the unreviewed costs which would result in a 15.58 percent disallowance; (2) The Commission could allow AFDC to be accrued on these unreviewed costs up until the time the costs are reviewed.

The Commission determines that neither alternative is acceptable. The first alternative has no basis in the record and the second alternative could result in a greater rate base inclusion in later years because of the carrying costs which would accrue from the date rates in this case are set until a new rate case is concluded and the appropriate amount placed into rate base.

Based on the foregoing, the Commission concludes that Public Counsel's adjustment should be rejected and that the unreviewed Callaway costs shall be included in rate base for purposes of this case. By allowing the costs in rate base, the Commission has made no findings with regard to prudence as the issue was not presented. As a result of this finding, the Company should withdraw its application in Case No. EO-86-36.

C. Employee Club

The Public Counsel proposes to disallow from rate base $259,000 associated with the Company's Employee Club. This adjustment also excludes certain expenses and taxes associated with this facility. The Company opposes Public Counsel's adjustment.

The Club is located in Valley Park overlooking the Meramec River. It consists of a log cabin, meeting building, house for the groundskeeper, outdoor pavilion, dance pavilion, dining hall and sports facilities. The Employee Club is used on evenings and weekends by employees and their families for social and recreational purposes. Senior citizens are bussed in daily throughout the summer. Dinner meetings are held for the general executive staff and company affiliated groups. In addition, other business meetings, seminars and employee training are held in the log cabin and large meeting buildings.

Public Counsel contends that the Club is used primarily for recreational purposes and the costs associated with the Club are not necessary for the provision of safe and adequate service. Therefore, the cost should be excluded.

Although the Company concedes that the Club is used for recreational purposes it produced evidence that it is being used increasingly for business meetings and employee seminars.

In Case No. ER-82-52, Re: Union Electric Company, 25 Mo. P.S.C. (N.S.) 194 (1982), the Commission disallowed costs associated with this facility on the ground that no evidence was produced to show that the facility represents a reasonable and necessary cost of rendering service and that the facility's role as a site for Company functions appeared to be secondary.

No evidence has been produced in this case which would lead to a different result. The Employee Club is used primarily for recreational purposes and any use for business purposes appear to be secondary. Accordingly, the Commission concludes that the Public Counsel's adjustment should be adopted as no evidence exists to show that the Employee Club is a necessary and reasonable business expense.

D. Fuel Inventory

The Staff included in rate base nuclear fuel inventory existing at year end 1986. The Company proposed an adjustment to this amount based upon the Company's 1987 test year fuel inventory which was a calculation of a 13-month average of balances of unburned fuel in the reactor. The Company has abandoned that calculation and proposes that the Commission average the fuel balance at the beginning of the fuel cycle with that which is projected to exist at the end of the fuel cycle. The average of these two numbers is $83.55 million.

Staff's $82.8 million figure is the actual amount existing in inventory at year end 1986 which is the midpoint of the 18-month Callaway refueling cycle. The Commission believes that this is the appropriate amount to use since it is an actual figure as opposed to the Company's average which is based upon a projected number. Accordingly, the Commission determines that Staff's fuel inventory calculation is reasonable and should be adopted.

E. Prepaid Pensions

Staff excludes average prepaid pensions from prepayments, while the Company proposes to include average prepaid pensions of $567,000 for 1986.

The appropriate amount of prepaid pensions is treated as an asset and made a part of the Company's rate base. Under FAS 87 the amount of pension expense for books and financial and reporting purposes was $10.9 million for 1986. Under the Employment Retirement Income Security Act of 1974 (ERISA) the minimum funding requirement for prepayments ranged from 0 to $14 million for 1986. The Company's actual contribution to its pension program was $13.4 million. This figure was based on the Company's actuarial report which in turn was based on FAS 87, ERISA requirements, and UE policy. The UE policy is to:

> fund the sum of the normal cost and the amount required to amortize the unfunded actuarial accrued liability over 15 years from January 1, 1986, plus interest, on the preceding items to the date contributions are made (assuming middle of year). (Exhibit 60, page III-3).

The effect of Staff's adjustment is to exclude the recognition of any amount in excess of that allowed by FAS 87 (the difference between $13.4 and $10.9 million), since ERISA would support a contribution of zero.

In the Commission's opinion Staff has not succeeded in showing that the Company's inclusion of average prepaid pensions for 1986 is unreasonable. The contribution was calculated on the actuarial report based on ERISA, FAS 87 and Company policy. Nowhere in the record is there any showing that the Company's funding policy is unreasonable. Accordingly, the Commission concludes that the Staff's position should be rejected and Company's rate base adjustment should be accepted.

III. Expense Issues

A. Fuel

1. 1986 Vs. 1987 Burned Cost

Staff uses actual 1986 test year fuel prices to calculate fuel expense. The Company uses 1987 projected fuel cost based on three months actual and nine months budgeted data. Staff and Public Counsel oppose the use of projected fuel prices.

The record reflects that fuel prices for the first six months in 1987 were lower than the same period in 1986, that Callaway fuel prices are expected to decline in 1987 and 1988 and that the spot prices and contract prices for coal have declined from June, 1986 to June, 1987.

In recent cases the Commission has recognized that the purpose of allowing forecasted fuel prices is to give the Company an opportunity to recover its fuel costs during periods of rapidly growing inflation. See Case No. EO-85-185, Re: Kansas City Power & Light Company, 75 P.U.R.4th 1, (1986), 28 Mo. P.S.C. (N.S.) 228 and Case No. ER-85-265, Re: Arkansas Power & Light Company, 74 P.U.R.4th 36, 28 Mo. P.S.C. (N.S.) 435 (1986).

This reasoning is still applicable given current conditions. The Company is experiencing no imminent threat of increased fuel prices. Accordingly, the Commission concludes that the test year 1986 level of fuel prices as proposed by Staff is appropriate and should be adopted in this case.

2. Hydro generation

Staff used a 1986 level of hydro generation in its fuel calculation. The Company normalized hydro generation based upon its contention that test year hydro generation was abnormally high. The Company maintains that 1986 hydro generation was 30 percent above normal because of abnormal rainfall. The Company has provided no other competent and substantial evidence to support its normalization adjustment.

It is difficult to accept Company's argument when it also claims that the years 1985, 1986 and 1987 have produced above normal hydro generation levels.

The 1986 hydro generation level approximated the average over the last five years and was 20 percent below the 1985 level. The Commission determines that the test year amount is reasonable as it is consistent with the 1982-1987 five-year average which is the period prior to the opening of the Truman Dam. Accordingly, the Commission finds that UE's normalization adjustment should be rejected.

3. Availability Of Fossil Plants

Staff uses actual test year availability rates for fossil plants, while Company normalizes the test year availability rates for lower than normal forced outage rates.

Staff opposes Company's adjustment on the ground that Company did not adjust for scheduled outages which were higher than normal. Staff contends that the test year level is normal since it is consistent with goals the Company has set for the 1987-1991 time period.

Although the Company should have taken into consideration scheduled outages as well as forced outages, the Commission determines that Company's availability rates are more reasonable than Staff's. Staff's availability rates for the Company's three main coal units are significantally higher than the 1984-1985 average, the 1981-1985 average and the Company's projected 1987-1996 availability rates. The Company's availability rates are consistent with the two year average, the five year average and the ten year forecast. Based on the foregoing, the Commission determines that Company's normalization of the 1986 test year availability rates should be adopted.

4. Pricing Of Incremental Sales

Staff and Company have stipulated to a kwh test year sales figure which is higher than 1986 actual sales. Staff and Company disagree concerning the method of

calculating the cost of generating the incremental sales. Company proposes that the cost be based upon average burned costs excluding Callaway generation while Staff contends that average burned costs including Callaway should be used. Company's position is based on the theory of economic dispatch. The theory assumes that the lowest operating cost plant will be dispatched first and incremental load will be met with higher cost plants. Since Callaway is the Company's lowest cost plant, Company argues, incremental load will be met with higher cost plants and therefore the incremental sales should be calculated excluding the Callaway generation.

Staff does not quarrel with the theory of economic dispatch. However, Staff points out that Callaway was voluntarily curtailed during the test year and this curtailment would satisfy 42 percent of the incremental load. In addition, Callaway was down for refueling in 1986. Finally, system burned costs for the 12 months ended June, 1987 are lower than system burned fuel costs for the 12 months ended June, 1986 even though sales have increased.

In the Commission's opinion, Staff has shown that the use of the average burned cost, including Callaway, is reasonable for the purposes of setting fuel cost for incremental sales. The voluntary curtailment of Callaway rebuts Company's argument that Callaway was operated to its full extent during the test year. Therefore, the Commission finds that average burned costs, including Callaway generation, should be used to calculate incremental sales for purposes of this case.

B. Advertising - Staff Issues

1. Introduction

In recent cases the Commission has categorized advertisements into five categories providing for separate rate treatment for each category. The five categories are:

1. General - Informational advertising that is useful in the provision of adequate service;

2. Safety - Advertising which conveys the ways to safely use electricity to avoid accidents;

3. Promotional - Advertising to encourage or promote the use of electricity;

4. Institutional - Advertising used to improve the Company's public image;

5. Political.

The reasonable cost of general and safety ads are includable in the cost of service, the cost of institutional or political ads are not includable in the cost of service and the cost of promotional ads are includable only to the extent that the utility can provide a cost justification for the ads. See Re: Kansas City Power & Light Company, 75 P.U.R.4th 1, 28 Mo. P.S.C. (N.S.) 228 (1986) KCPL and Re: Arkansas Power & Light Company, 74 P.U.R.4th 36, 28 Mo. P.S.C. (N.S.) 436 (1986).

In this case Staff has excluded the costs of advertising which it deems to be promotional and certain advertising which it deems to be institutional.

2. Promotional Advertising

Staff has excluded $73,000 associated with promotional advertising. These are largely heat pump ads which promote the use of electricity during off-peak times.

Although the Company's evidence shows that expenses associated with promotional heat pump advertising have been exceeded by revenues received because of the sale of heat pumps, the Company has not shown a causal connection between heat pump advertising and increased revenues. It is just as likely that heat pump sales are a result of factors unrelated to heat pump promotions.

In the Commission's opinion the Company has not shown a causal relationship between its heat pump advertising expense, heat pump sales and increased revenues. Similarly, the Company has not shown a cost justification for its other off-peak load building promotions. Accordingly, the Commission concludes that Staff's adjustment should be adopted.

3. Institutional Advertising

Staff has excluded approximately $13,000 associated with institutional advertising. Staff has presented very little evidence in support of its adjustment.

Since Staff has not produced or described the advertisements it seeks to exclude. Its evidence amounts to little more than conclusory statements that Staff deems the advertisement to be of the type properly classified as institutional.

Company contends that the advertisements addressed cooling tips, weatherization, special billing programs, temperature setting, storm restoration, and its commitment to good service. Although the last category would fall into an excludible category, no quantification of these categories has been produced.

In the Commission's opinion, Staff has the burden of proof on this issue and it has failed to produce sufficient evidence to support its exclusion.

Based on the foregoing, the Commission concludes that Staff's adjustment related to institutional advertising should be rejected.

C. Advertising - Public Counsel Issue

Public Counsel has disallowed $14,960 associated with five advertisements appearing in the Manager's Column. The Manager's Column is published in the newspaper on a monthly basis.

Company originally classified these ads as general, but now the Company concedes that four of the ads should be excluded as institutional. Company contests one ad which informs the public about the Company's Speakers Forum. Company contends that safety is often a topic at the Speakers Forum.

The Commission having reviewed the advertisement finds that it should be classified in the general and safety categories. The subjects described in the ad primarily relate to safety, information about electricity and weatherization.

Based on the foregoing, the Commission concludes that the advertisement associated with the Speakers Forum should be included. Accordingly, Public Counsel's adjustment should be reduced by one-fifth.

D. Management Audit

The Company proposes to include in cost of service $873,000 associated with the management audit. Staff opposes this adjustment without an offsetting amount to

reflect savings associated with the audit. In addition, Staff contends that if the amount were included a jurisdictional allocation should be made to this expense.

Staff maintains that the cost has been paid and is therefore a nonrecurring expense. In addition, Staff argues that the savings associated with the audit are expected to exceed the cost of the audit and therefore it is improper to include the cost without the offsetting savings. Finally, since all jurisdictions will benefit from the management audit savings, a jurisdictional allocation should be applied to any costs allowed.

In Case No. EO-84-73, the Commission, at Staff's request, ordered a management audit of the Company which was performed by Arthur Young. Staff's request contained the recommendation that the Company be allowed to recover the reasonable costs of the management audit in future rates. In the Commission's opinion, it would be inequitable to order a management audit of the Company and then deny recovery of the expense. The Commission rejects Staff's argument with respect to its proposed savings offset as any savings occurring in the test year will be reflected in the rates set in this case and savings in future test years will be reflected in future rates. However, since the expense is a one-time nonrecurring expense, the Commission believes that it is appropriate to amortize the cost over three years. Therefore, the Commission finds that the cost of the management audit should be included based on a three-year amortization.

E. Management Salaries

Staff has adjusted the annualized 1986 wages by $1,400,000 to reflect a reduction to management salary increases. Company opposes this adjustment.

During the test year, authorized salary increases for Company employees was 6.42 percent for management employees and 4.25 percent for union employees. The Company's salary administration and research department provides salary recommendations to upper management. The recommendation is based on a job evaluation study performed by an outside consultant. The study indicated that UE salaries were

4 percent deficient of the Company's goal to be in the 50th percentile for wages paid for electric companies in the same revenue class as UE. The Company intends to reach the goal over a four-year period beginning with 1984. In addition, based upon the job evaluation study, UE established parity in salary between former Union Electric management salary levels and former subsidiary management salary levels.

Staff contends that UE has minimal turnover as a result of inadequate compensation and therefore the validity of the Company's study is suspect. Staff also contends that there is no justification for bringing management employees of the former subsidiaries into parity with the former UE management.

Because Staff questions the Company's study and the reasonableness of the parity adjustment, it contends that no increase is justified. However, Staff has recommended that management salary increases be included which are equal to the salary increases granted to union employees of 4.25 percent.

In the Commission's opinion Staff has not met its burden of proof on this issue. It appears to have based its entire recommendation on the fact that UE has minimal turnover. Although turnover is one factor to consider in assessing the reasonableness of management salaries, it is not the only relevant factor. The Company's salary increases are based on a study performed by an outside consultant and attempts to reach what appears on its face to be a reasonable goal. To meet its burden of proof, Staff would be required to produce persuasive evidence that the Company's salary study is unreliable, resulting in unreasonable salary adjustments.

Based on the foregoing, the Commission determines that Staff's adjustment to management salaries should be rejected.

F. Management Incentive Plan

Company includes the management incentive plan as an expense in cost of service. Staff opposes this adjustment.

The Company proposes to include $1,186,000 in Missouri jurisdictional cost of service for its management incentive plan. This amount is based on the assumption

that six of seven goals will be attained. For each goal achieved, management employees will receive a bonus of .3 percent over their base salary. The goals of the plan are as follows:

1. Reduce preventable motor vehicle accidents by 10 percent, and achieve a specific level of on-the-job accidents.
2. Achieve a five percent reduction in sick leave.
3. Limit O&M expenses to the budgeted level.
4. Limit construction expenditures to a specified level.
5. Achieve a five percent reduction in customer outage time.
6. Achieve a five percent reduction in the level of non-Callaway materials and supplies inventory.
7. Achieve an overall major power plant equivalent availability rate of 73 percent.

Staff opposes this adjustment on three grounds: (1) the Company has not determined the savings resulting from the plan and has made no offset to the cost of the plan by such savings; (2) there is no guarantee that the Company will incur the cost associated with the plan; and (3) only four of the seven goals call for improvement over 1986 performance.

The Commission believes that programs designed to improve management performance should be encouraged and is not opposed, in principle, to cost of service recovery of the costs associated with such programs. However, the Staff's criticism of the Company's plan for ratemaking purposes is well taken. At a minimum, an acceptable management performance plan should contain goals that improve existing performance, and the benefits of the plan should be ascertainable and reasonably related to the incentive plan. The Company's management incentive plan meets neither of these minimum standards. Accordingly, the Commission determines that the Company's adjustment should be rejected.

G. 1987 Wage Annualization

The Company proposes to adjust test year wages by $8,524,000 to reflect a 4.5 percent budgeted salary increase effective July 1, 1987. The Staff includes only 1986 wage increases.

Since the Commission has determined that the 1986 test year will be used for purposes of this case, it will not accept isolated adjustments beyond the test year without persuasive justification.

At the time this adjustment was proposed, it was based on a budgeted amount and therefore was not known and measurable. Because the evidence shows that Company's cost of service is more likely to decline than to increase subsequent to the 1986 test year, the Commission has determined not to true-up for items which increase costs but do not consider offsetting decreases. Accordingly, the Company's adjustment shall be rejected and its motion to reopen the record to address wage increases shall be denied.

Based on the foregoing, the test year level of wages shall be used for purposes of this case.

H. 1987 Annualization Of Pensions And Benefits

The Company proposes to increase pensions and benefits by approximately $4.6 million. In the Commission's opinion the Company's adjustment fails to preserve the integrity of the test year and in addition is not known and measurable. The evidence shows that benefits expense for the first six months of 1987 are less than for the same time period in 1986. This is true without considering certain abnormal medical expenses which were adjusted out of the 1986 test year. The pension costs are expected to be similar to amounts paid in 1984, 1985 and 1986. However, Company contends that they will increase somewhat to reflect retirement benefits and lower amounts charged to construction.

The Commission is not persuaded that any increases in pensions and benefits beyond the test year should be adopted as the reasonableness of these increases has

not been shown and, therefore, persuasive evidence has not been advanced to justify increasing these amounts beyond the test year without reflecting offsetting decreases.

I. 1987 EPRI Payments

The Company proposes to reflect the 1987 EPRI payment of $188,000.

No persuasive evidence has been advanced by the Company in support of this adjustment as it is merely another attempt to increase cost of service without reflecting offsetting decreases to cost of service.

J. Replacement Power Insurance

The Company seeks recovery of the cost of premiums paid to Nuclear Electric Insurance Limited (NEIL) for replacement power insurance. Staff excludes $459,000 from cost of service on the ground that no justification exists for the coverage.

NEIL is an organization which insures nuclear power plants. Pursuant to the terms of the policy, in the event of an accidental outage, NEIL will pay for replacement power commencing 26 weeks after the outage occurs. The policy provides that NEIL will pay $1.5 million per week for the first year. If NEIL has insufficient funds to pay for a recoverable outage incurred by one of its clients, the Company could be subject to a retroactive assessment of $2.8 million. This amount can be assessed no more than once every year.

In a recent case involving the Kansas City Power & Light Company, the Commission disallowed the same expense on the ground that it was not in the interest of the Missouri ratepayers to subject them to the potential payment of additional expenses to cover claims of other companies. In addition, the Commission expressed the opinion that an outage of 26 weeks or more was not likely to be a frequent occurrence. See Re: Kansas City Power & Light Company, 75 P.U.R.4th 1, 140, 28 Mo. P.S.C. (N.S.) 228, 385 (1986). Company contends that the retroactive assessment would not be for the purpose of directly paying claims of other companies. Rather, the assessment is to hold premiums down unless and until losses exceed the company's

financial resources. In the Commission's opinion, whether directly or indirectly, the retroactive assessments are related to the risks associated with the claims of other utilities.

The Company also argues that the premium is reasonable because it has recovered 124 percent of its insurance premiums on fossil plant outages over the past ten years. This argument is not persuasive as there is no showing that fossil and nuclear plants are similar with respect to outage experience, insurance premiums, and conditions of recovery under such policies.

In the Commission's opinion, no evidence has been presented to lead the Commission to deviate from its finding in KCPL, supra, on this issue. The record is devoid of any evidence which would show the reasonableness of incurring a potential $2.8 million assessment. The evidence does not suggest that the probability of an outage exceeding 26 weeks justifies the risk of the assessment.

Based on the foregoing, the Commission concludes that the cost of insurance premiums to NEIL should be excluded from cost of service.

K. Harris Litigation

Staff proposes to reduce the Company's expenses by $3,826,000 associated with the amount of the judgment, plaintiff's attorney fees and Company's attorney fees in the "Harris litigation". The Harris litigation involved a securities fraud action brought against UE by a class of bondholders. This action resulted from the Company's attempt to call certain first mortgage bonds.

In April, 1978, UE attempted to call $50 million Series 2005 First Mortgage Bonds which were issued in 1975. The bonds bore an interest rate of 10.5 percent and contained a "ten year no call" provision. Under the provision, the bonds were not redeemable prior to March 1, 1985, if the funds for redemption were borrowed at an interest cost of less than 10.60 percent per annum. However, the restriction was not applicable if the money used in the redemption came from the improvement or

maintenance funds established by the supplemental indenture which created the 10.5 percent bonds.

In lieu of cash deposits in the maintenance and improvement funds, the Company could use 60 percent of the value of property additions to satisfy the requirement. The Company followed this procedure.

In April, 1978, the Company obtained approximately $50 million of short-term debt at less than 10.5 percent and deposited the amount in the maintenance and improvement funds. The Company intended to use the funds to redeem the $50 million principal amount of bonds and replace the short-term debt by first mortgage bonds bearing a 9.35 percent interest rate.

On April 11, 1978, the Company publicly announced its intent to call the bonds. As a result of the announcement, the market value of the bonds dropped $120 per bond. The trustee of the Series 2005 bonds would not issue the call order until judicial approval was granted because it questioned the legality of the plan to call the bonds through UE's maintenance fund. On May 9, 1978, the bondholders initiated a state court action against UE and its trustee. When the purchasers of the replacement long-term mortgage learned of the litigation, they refused to buy the bonds. As a result, UE dropped the call provision of the Series 2005 bonds and discontinued use of the short-term debt.

In February, 1980, Harold Harris, Continental Causality Company and National Fire Insurance Company, individually, and on behalf of a class of bondholders, instituted a federal class action against UE alleging violation of Section 10(b) of the Securities Exchange Act and Rule 10(b-5) of the Securities Exchange Commission. The plaintiff prevailed in the district court winning a jury verdict of $2,716,240 against the Company. The case was appealed to the Eighth Circuit Court of Appeals which issued a decision affirming the District Court's judgment holding that:

> ...the evidence is sufficient for the jury to have found that UE's entire conduct from March, 1975 to April, 1978 concerning the Series 2005 Bonds constituted a course of business and scheme or artifice which operated as a fraud on the bondholders. Harris v. Union Electric Company, 787 F.2d 355, 362 (8 Cir. 1986)

In support of its adjustment, Staff argues that litigation costs and damages associated with a judicial decree based on a utility's unlawful conduct, should be presumed unreasonable. In addition, Staff contends that the Company's action provided little or no benefit to the ratepayers and, therefore, should be disallowed.

The Company contends that the litigation costs are a reasonable business expense and that its attempt to call the bonds were aimed at reducing its cost of money which if successful would have been beneficial to ratepayers.

In the Commission's opinion, the Company has not shown that its action underlying the litigation was prudent and, therefore, has not shown the inclusion of these litigation expenses to be justified.

The Company was not being pressured by this Commission to redeem the bonds in question. The Company had intended and represented that the bonds contained a no call provision. The Company was aware that its action carried a substantial risk of litigation initiated by the bondholders as is evidenced by a letter written to a company executive by one of UE's directors in opposition to the action. It is apparent that a serious doubt existed as to the legality of the redemption attempt.

Based on all the foregoing considerations, the Commission determines that the consequences of the substantial risk taken by the Company regarding the events leading up to this litigation should be placed on the shoulders of the shareholders and not Missouri ratepayers. Accordingly, the Commission concludes that Staff's adjustment should be adopted.

L. Legal And Special Services

The Staff proposes to disallow the test year expenses related to the defense of certain antitrust cases by the Company. The Missouri jurisdictional amount of these expenses was $608,000.

Staff does not allege that these expenses were unreasonable or imprudently incurred. Rather, Staff argues that since the litigation involves a dispute over FERC's tariffs, the cost should be assigned to the FERC jurisdiction and not to the Missouri ratepayer.

The Commission does not believe it is an appropriate ratemaking technique to directly assign this type of expense to specific jurisdictions. It is undesirable to start a precedent toward this kind of direct assignment as it would be likely to encourage additional disputes regarding jurisdictional allocations and could cause administrative problems related to the assignment of these expenses.

Based on the foregoing, the Commission determines that these expenses should be assigned based on the jurisdictional allocation factor. Accordingly, the Commission finds that Staff's adjustment should be rejected.

M. Injury And Damages Reserve

Public Counsel proposes a normalization adjustment for injury and damages expense. Based upon the exclusion of expenses associated with the Harris issue, this normalization reduces injury and damages expense by $197,000. Company opposes this adjustment.

The Public Counsel witness examined the three categories of injuries and damages expense, Workmen's Compensation claims, medical claims and public claims. The witness chose the 1984-1986 period as historical periods to determine a proper normalization amount. This period was chosen because it represents the period subsequent to the merger of Union Electric and its subsidiaries. In the area of Workmen's Compensation claims, the witness determined that since the payments increased in each of the three years, the use of 1986 levels would be more

appropriate than an average. In the area of medical claims, the expense had fluctuated with 1985 being the highest and 1984 being the lowest. Based upon this experience, the witness averaged 1985 and 1986 to arrive at a normalization adjustment for this category. In the area of public claims, the witness used a simple average of three years because the amount fluctuated during the years with 1986 being the highest followed by 1984 and 1985 being the lowest.

Although Company provided no evidence on this issue, it argues in its brief that since the injury and damages reserve is based upon estimated claims, it is already normalized.

The Commission can find no support for Company's claim that the injury and damages reserve is normalized when the injury and damages reserve under the Company's case, including the Harris litigation, amounts to $7,170,000 in contrast to Public Counsel's normalized level, including Harris, of $3,925,802.

In the Commission's opinion it is appropriate and a common ratemaking practice to normalize expenses which fluctuate from year to year. Public Counsel has shown this to be the case respecting these expenses. In addition, Public Counsel's adjustments are reasonable based upon a review of the Company's experience since the UE merger.

Based upon the foregoing, the Commission concludes that Public Counsel's normalization adjustment to the injury and damages expense is appropriate and should be used for purposes of this case.

N. Residential Insulation Plan

The Staff proposes to increase Company's cost of service by $63,000 to reflect the amount of interest expense associated with the residential insulation plan (RIP). The Company asserts that this amount should be $225,000 pursuant to the Stipulation and Agreement between Company and Staff in Case No. ER-81-180.

In that Stipulation, the Company agreed to a modification of its residential insulation financing program which resulted in the Company agreeing to

loan money at the rate of 5 percent up to a total of $2.5 million. Staff contends that in the 1981 Stipulation, $225,000 was included in rates to allow the Company to recover the difference between the interest rate charged to customers under the prior insulation financing program (14 percent) and the new rate of 5 percent, a 9 percent difference.

In Case No. ER-82-52, Staff proposed to reduce the amount in cost of service to $143,000. Based on the amount of outstanding loans at the time ($1,100,000), Staff's proposed adjustment was designed to allow the Company to recover the difference between the existing interest rate and the five percent RIP interest rate on the outstanding balance. The difference was 12.69 percent. The Commission rejected this proposal on the ground that it was likely that the full $2.5 million would be committed in the future.

In this case Staff recommends $62,857 which is based on the difference between the prime rate at December 31, 1986 and the RIP rate of 5 percent, a difference of 2.5 percent. Staff applies the 2.5 percent to the amount committed at December 31, 1986 ($2,514,286).

Since the record reflects that the full $2.5 million amount has been committed, the Commission is of the opinion that it is reasonable for the Company to recover in cost of service only the cost to it of financing the amount in excess of 5 percent as applied to the total amount of the program ($2.5 million). Even though the Company asserts that the prime rate has changed, the evidence in this case shows that the Company can borrow short-term debt at 7 percent, a difference of 2 percent. Thus, Staff's 2.5 percent figure is reasonable.

This result is not inconsistent with the Commission's finding in Case No. ER-82-52. In that case Staff's request was clearly unreasonable in light of the following: the difference was 12.69 percent, an amount greater than the 9 percent originally contemplated and the loans had not been committed to the full $2.5 million amount.

Based on the foregoing, the Commission finds that Staff's adjustment should be adopted.

O. Nonfuel Production O&M

This issue involves a proper classification of nonfuel production operation and maintenance (O&M expense). The question is whether this expense should be classified as demand related (fixed) or energy related (variable). The appropriate classification determines whether the demand or energy allocator is applied to these expenses for purposes of jurisdictional allocations.

In its filed testimony, Company classified these expenses as mostly variable and, therefore, allocated them based upon the energy allocator. Subsequent to the filing and prior to the hearing, Company accepted Staff's method of classifying these expenses as demand related. Public Counsel's classification is different from Staff's primarily in the treatment of maintenance expense accounts. In support of the reasonableness of its allocation, Public Counsel contends that maintenance expenses, in general, are energy related, since more regular maintenance is required the more the units are run. Public Counsel also points to the fact that this method is consistent with the NARUC Electric Utility Cost Allocation Manual.

This issue was presented in Case No. ER-82-52 where the Company had classified these costs as variable but subsequently agreed with Staff's method of classification. Public Counsel took the position that this expense should be classified as variable. In that case, the Commission issued a Supplemental and Correction Order addressing the issue finding as follows:

> In the Commission's opinion there is no competent and substantial evidence to support the Staff's determination of variable costs and that position cannot be maintained. The only competent and substantial evidence on this issue has been presented by Company witness Wucher and Kovach. The variable expenses described by Wucher and Kovach, enumerated above, should be included in the variable costs to be allocated. That result is consistent with the Commission's Report and Order in the Missouri Public Service Company case, ER-82-39, in which the Commission found that all increases in production operation and maintenance expense should

be spread on a kwh basis since those costs increase as production increases. Re: Union Electric Company, ER-82-52, Supplemental and Correction Order, 22 Mo. P.S.C. (N.S.) 442, 447 (1982).

On the other hand, in two recent cases the Commission has allocated these expenses on a fixed basis. See Re: Kansas City Power & Light Company, ER-82-66, 25 Mo. P.S.C. (N.S.) 229, 251 (1982) and Re: Arkansas Power & Light Company, ER-85-265, 74 P.U.R.4th 36, 63, 28 Mo. P.S.C. (N.S.) 435, 465 (1986). In both of those cases evidence was in the record supporting Staff's position which the Commission found persuasive.

The only testimony in support of Staff's position is its reliance on a Company pricing study related to the pricing of interchange sales which makes the following statement: "incremental maintenance costs are constant". Based on Public Counsel's cross-examination, it is not at all clear that this statement means maintenance expense does not vary with generation levels. The only other evidence in support of Staff's position is the Staff witness' conclusory statement that "...you will not see and I have never seen any example that will show that maintenance costs move in direct relationship with the production levels of the power plant". (Tr. 611)

In the Commission's opinion Public Counsel's position is appropriate for purposes of this case. Public Counsel's method has been consistently used by Union Electric Company since 1974, and it is reasonable to assume that maintenance costs do bear a relationship to kwh output absent any persuasive evidence to the contrary. Accordingly, the Commission concludes that Public Counsel's position with respect to nonfuel production O&M should be adopted.

P. PSC Assessment

During the course of the hearing, Public Counsel proposed that the Commission adopt the 1987 level for the Company's PSC assessment. However, Public Counsel has abandoned this position. Therefore, the parties agree that an adjustment of a negative $129,006 should be made to the 1986 test year expense in order to

annualize the amount paid by Union Electric in 1986 for its PSC assessment. The Commission determines that this adjustment is appropriate.

Q. EEI Dues

Public Counsel reduces Company's cost of service by $280,000 to reflect dues paid to the Edison Electric Institute (EEI) and certain EEI expenses charged to public relations expense.

This Commission has consistently excluded EEI dues from cost of service for the last several years on the ground that these payments have not been shown to produce any direct benefit to the ratepayers. Recently the Commission has stated that not only must a direct benefit be shown but the benefits must be quantified and allocated between shareholders and ratepayers. See Re: Kansas City Power & Light Company, 75 P.U.R.4th 1, 32, 28 Mo. P.S.C. (N.S.) 228, 259 (1986).

The Commission continues to adopt this standard as reasonable for the inclusion of EEI dues in cost of service. The Company's testimony includes a list of benefits which it alleges have resulted from EEI membership. No quantification or allocation of EEI benefits appear in the Company's testimony other than the hearsay statement that 20 percent of EEI activities are devoted to lobbying.

Since the Commission's standard has not been met for the inclusion of EEI dues in the Company's cost of service, the Commission concludes that EEI dues should be excluded from cost of service as proposed by the Public Counsel.

R. Three Mile Island

Public Counsel contends that the amounts paid for the Company's contribution to the Three Mile Island (TMI) clean-up costs should be eliminated from cost of service. This adjustment reduces cost of service by $286,000. The Company opposes this adjustment.

This issue involves payments to a fund administered by EEI to be used to pay for the clean up of the damaged reactor at Three Mile Island. Company contends

numerous benefits have been derived from this clean-up program such as improved knowledge concerning safety and decontamination techniques.

In the Commission's opinion this knowledge can be obtained through other means. To ask the Missouri ratepayers to fund the clean up of the Three Mile Island nuclear accident is clearly unreasonable. The Commission finds that Public Counsel's adjustment should be adopted.

S. Trade Associations and Public Service Organizations

Public Counsel proposes an adjustment of $23,000 to remove the Company's expense related to its payment to the Committee For Consistent Accounting Practices (CCAP) concerning proposed amendments to FAS statement 71. Public Counsel also removes $1,000 of expenses related to trade associations and public service organizations which include the Society of Industrial Realtors and the Press Club of Metropolitan St. Louis. Company opposes Public Counsel's adjustments.

The Company contends that the lobbying purposes of the CCAP was to lobby FASB regarding the potentially deleterious effects on utility companies, ratepayers and regulators which could result from the proposed amendment to FAS 71.

The record does not show what effect these lobbying activities have had on Missouri ratepayers. It is unknown whether they were effective and in fact benefited Missouri ratepayers. In addition, there is no quantification or allocation of these alleged benefits between the ratepayers and shareholders. Since the evidence does not show the benefit of these activities to Missouri ratepayers the Commission concludes that these expenses should be excluded and Public Counsel's adjustment should be adopted.

With respect to the other trade associations and public service organizations, the Company produced no evidence in opposition to Public Counsel's adjustment. These adjustments on their face appear to be reasonable and therefore should be adopted in this case. Accordingly, payments made to trade associations and

public service organizations should be excluded from cost of service as proposed by Public Counsel.

T. Public Relations Expense

1. Social And Civic Activities

Public Counsel excludes approximately $12,000 in expenses associated with social activities, social clubs and civic activities. The Company has provided no evidence contesting this adjustment.

Expenses in this category have been traditionally excluded from cost of service since such activities provide no quantifiable benefit to ratepayers. The Commission concludes that these expenses should be excluded.

2. Acid Rain

Public Counsel has excluded $44,000 of expense which represents payments to the Citizens for Sensible Control of Acid Rain (CSCAR).

Company contends that this expense funds a lobbying effort which will benefit ratepayers since expensive acid rain legislation will be detrimental to them.

The Commission is of the opinion that any direct benefit to ratepayers as a result of these lobbying efforts is unknown. Therefore, any benefits to ratepayers associated with this effort is purely speculative. Since no benefits or quantification of benefits have been shown and no allocation of these alleged benefits between shareholders and ratepayers have been produced, the Commission determines that these expenses should be excluded.

3. Cambridge Reports

Public Counsel proposes to disallow the cost of two surveys funded by UE regarding customer attitudes. Public Counsel contends that these surveys are analogous to institutional advertising since they are designed to promote a better public image.

The Company produced evidence describing some of the questions contained in the survey. The inquiries concern budget billing, credit counseling, thermostat

setting, whether customers have control over their usage and customer opinion as to the Company's rates.

The Commission is unable to find, based on the evidence presented, that these surveys are aimed solely at improving the Company's image. It appears that the surveys are designed to provide useful information to the Company which could assist it in providing service and effective programs for its customers. Therefore, based upon the evidence before it, the Commission is of the opinion that these expenses appear to be a reasonable business expense.

The Commission finds that the expenses associated with Cambridge Reports should be included in the Company's cost of service for ratemaking purposes.

IV. Taxes

A. Property Taxes

Staff proposes a reduction to property taxes of $2,884,000 to remove the property taxes associated with the disallowed portion of the Callaway plant. Company opposes this adjustment.

It was established on cross-examination that property taxes are assessed based on the consideration of three factors: the cost of the property; the Company's income; and the market value of the Company's stock. Although the cost of the property might reflect the disallowed portion of the plant it is likely that the Company's income and the market value would not include the disallowed portion.

Staff does not know what method was used or whether the valuation already reflects the disallowed portion of the plant. In the Commission's opinion the Staff has not met its burden of proof, since Staff has failed to establish that the Callaway property tax assessment includes an assessment on the disallowed portion of the plant.

Based on the foregoing the Commission concludes that Staff's adjustment should be rejected.

B. Franchise Taxes

Staff opposes a reduction to corporate franchise taxes of $156,000 which reflects the use of 1987 corporate franchise taxes and the removal of corporate franchise taxes on the disallowed portion of the Callaway plant and plant held for future use. Company opposes this adjustment.

There is no dispute that the disallowed cost of Callaway were included in the basis on which this tax was calculated. In the Commission's opinion, it is reasonable to disallow the portion of taxes which are attributed to the Callaway plant which is not included in rate base. These costs have been disallowed because of a finding of imprudence and therefore the ratepayers should not be charged the expense which is associated with that portion of the tax.

Although Company states Staff's use of the 1987 tax bill to calculate franchise taxes is inconsistent, the Commission believes that the Company has no basis to complain since the use of the known and measurable 1987 tax rate results in a smaller adjustment than originally calculated by Staff in its prefiled testimony, thereby increasing the revenue requirement. Based on the foregoing, the Commission concludes that Staff's adjustment is reasonable and should be adopted.

C. Contributions In Aid Of Construction

The Public Counsel contends that the Commission should declare that taxes associated with contributions in aid of construction (CIAC) be paid by the provider of the CIAC and not the general body of UE ratepayers. The Company suggests two alternatives for the treatment of CIAC.

The Staff recommends that the Commission defer any decision with respect to CIAC until UE files a CIAC tariff or until it requests rate relief to pay CIAC taxes.

The Commission is persuaded by Staff arguments. Since no party has proposed any revenue requirement adjustment associated with taxes on CIAC in this case, the Commission believes that CIAC should be addressed at a later time when all relevant issues relating to CIAC can be addressed and disposed of.

Based on the foregoing the Commission defers any decision with respect to CIAC treatment until UE files a CIAC tariff or until it requests rate relief to pay CIAC taxes.

V. Rate of Return

A. Capital Structure

The Company proposes a capital structure based upon actual data through July 31, 1987, with pro forma adjustments to September 30, 1987. As noted above, the Company proposes that the capital structure be trued up to September 30, 1987. The Staff uses a capital structure at December 31, 1986, adjusted for certain known and measurable changes.

The Company opposes the use of a December 31, 1986 capital structure. However, if the Commission uses the test year capital structure, the Company disagrees with two of Staff's adjustments: (1) the treatment of the retirement of certain preferred stock in February, 1987; and, (2) the write-off of Callaway I and Callaway II disallowed costs.

In the Commission's opinion, the use of a capital structure at December 31, 1986, is appropriate and is consistent with the Commission's finding regarding the use of the test year in this case. The Company's proposed 1987 capital structure is based on a projection and is, therefore, not known and measurable. In addition, the proposed capital structure extends nine months beyond the test year which has been used to establish rates in this case, thereby violating the matching principle. The Commission has rejected UE's request to true-up isolated items. This approach tends to distort the test year and mask the indications that cost of service is declining. Staff's adjustments to the capital structure are discussed below.

1. Treatment Of Preferred Stock Call Premium

On February 15, 1987, the Company redeemed all of the outstanding shares of an issue of preferred stock. The 3,000,000 shares of the $25 stated value preferred

stock paid a dividend of $12 million on an annual basis and bore a cost of 16.84 percent.

The Company redeemed the stock by paying a premium of $7,950,000 in excess of par value. To recognize this refinancing, Staff removed $75 million from the Company's capital structure and adjusted common equity to remove the $7,950,000 associated with the call premium paid on the retirement. The premium was paid out of retained earnings.

In contrast to Staff's treatment of the call premium, the Company proposes to amortize the premium over a ten-year period by adding it to the cost of outstanding preferred stock in the amount of $795,000 per year (one-tenth of $7,950,000). The unamortized balance would be included in the common equity portion of UE's capital structure. The Company contends that this method shares the benefits associated with the retirement between ratepayers and shareholders.

In the Commission's opinion, the Company's proposal is not reasonable. As a result of the redemption the Company was able to forego the dividends on the preferred stock which amounts to $12 million on an annual basis. The cost to redeem was $7,950,000 and the savings to the Company from February 15, 1987 through December 31, 1987, (the effective date of this Report and Order) is approximately $10,448,000. Therefore, the shareholders had a net gain of over $2,500,000 on the transaction during 1987. Thus, the shareholders have the benefit of these savings until new rates are set. The Commission believes that it is unreasonable to assign costs to preferred stock which do not exist or to artificially increase the equity portion of the capital structure under some proposed benefit sharing theory.

The Commission determines that it is reasonable to adjust the capital structure as proposed by the Staff. The retirement of preferred stock occurred approximately 45 days outside of the test year, it is known and measurable and it has a substantial effect on the Company's capital structure. Therefore, a persuasive

justification exists to adjust the test year capital structure to reflect the preferred stock refund.

2. Callaway I and Callaway II

Staff proposes to adjust the December 31, 1986, common equity balance by $223.9 million to reflect a write-off of disallowed Callaway I costs and by $53.5 million to reflect a write-off of disallowed Callaway II costs.

Company opposes this adjustment since it assumes a write-off in all jurisdictions of Callaway I. Company asserts that appeals are pending in the other jurisdictions. In addition, the Company contends that the 46 percent tax rate should be used in calculating the write-off rather than the current tax rate.

With respect to Callaway II, Company contends that the capital structure should not reflect this write-off since an appeal is pending concerning the disallowance.

The Commission notes that Staff's adjustment does not require the Company to write-off these amounts prior to the completion of any pending appeals. The adjustment merely assures that the capital structure reflects the fact that certain costs associated with Callaway I and Callaway II have been excluded from the Company's cost of service. In the Commission's opinion this adjustment is reasonable as the capital structure should not reflect costs which have been found to be excludible from rates.

Based on the foregoing considerations, the Commission finds that the capital structure to be used for purposes of this case is as follows:

Long-Term Debt	53.62%
Preferred Stock	9.60%
Common Equity	36.78%
	100.00%

B. Cost of Common Equity

There is no dispute as to the cost of long-term debt and preferred stock, 8.78 percent and 8.24 percent respectively. The current authorized return on equity is 15.62 percent. All parties agree that the cost of equity has decreased since the Callaway rate case. The Company, Staff and the Public Counsel produced witnesses who performed recommendations concerning appropriate return on equity for the Company.

Staff witness Shackelford performed a discounted cash flow analysis (DCF) to determine a recommended return on equity for the Company. The discounted cash flow model estimates the required return by using the current stock price, the expected dividend and an estimate of the growth rate. In the formula the expected dividend is divided by the stock price to produce a yield which is added to the growth rate. In addition, Shackelford used the capital asset pricing model. This formula measures the risk return relationship of a particular stock.

To determine the yield portion of the DCF formula, Shackelford observed market prices of UE's common stock from January, 1986 through March 20, 1987. His analysis showed that UE's stock prices have increased since January, 1986 but have leveled off since August, 1986. Mr. Shackelford noted that since the quarterly dividend increased in October, 1986, the yields have ranged from 6.39 to 6.72 percent. Based upon these trends, Shackelford used the time period October, 1986 to March 30, 1987, to develop his yield figure. Shackelford used a dividend per share figure of $1.96. The resulting dividend yield ranges from 6.52 to 6.86 percent.

To determine the growth term for the formula, Shackelford analyzed historical growth rates in dividends and earnings per share for the period 1975 through 1986, projected growth rates in dividends per share for the period 1987 to 1991 and projected growth in earnings per share for the period 1987 through 1990. Based upon this review, Shackelford used a growth rate ranging from 4.5 to 5 percent.

Shackelford's capital asset pricing model estimates a cost of equity of 12.29 percent. Based upon his DCF and capital asset pricing model, Shackelford

concludes that a reasonable range for cost of equity is from 11.5 percent to 12.4 percent. Shackelford's specific recommendation is 12 percent. His review of average DCFs and capital asset pricing model returns for a group of comparable companies indicates an average return ranging from 11.21 percent to 12.5 percent which Shackelford believes reinforces the reasonableness of his 12 percent recommendation.

In his rebuttal testimony, Shackelford updated his DCF analysis for the six months ended August 31, 1987. His calculation results in DCFs ranging from 10.77 to 12.88 percent with an average DCF of 11.88 percent. This updated DCF formula assumes a dividend of $1.98 and growth rates ranging from 4 to 4.5 percent. Shackelford changed the growth rate since Value Line had decreased estimated dividend growth rates from 4 percent to 3.5 percent and Merrill Lynch had estimated a long-term dividend growth rate at 2.1 percent. Mr. Shackelford's revised capital pricing model rates results in a range from 12.26 percent to 13.02 percent.

Public Counsel's witness Parcell performed DCF analyses and comparable earnings tests to estimate UE's cost of equity. His comparable earnings test indicates a cost of equity of 12.5 to 13 percent. Mr. Parcell recommends the lower range since it better recognizes recent trends of declining inflation, interest rates and capital costs.

Parcell performed a historic DCF calculation based upon five year average yields over the period 1982 to 1986. The average yield for UE is 10.5 percent. The 1986 yield was 7.1 percent. To estimate growth rates, Mr. Parcell used the earnings retention method and reviewed historical growth rates in dividends per share, earnings per share and book value per share. The average retention growth rate for UE was 5.4 percent and the historic growth rate averaged 3.8 percent.

Parcell's historic analysis indicates a DCF derived cost of equity ranging from 10.9 to 15.9 percent. Parcell recommends the 1986 yield figure since he believes it represents the most appropriate component for a current DCF analysis. This results in a return on equity ranging from 10.9 to 12.5 percent.

Parcell also performed a prospective DCF analysis to determine a DCF derived rate on a prospective basis. He used the current dividend rate and increased it by .5 of the expected growth rate. He uses the average stock price for UE and a comparison group of companies for the period January through March, 1987. He reviewed the retention growth rate, a 1989 to 1991 prospective earnings retention growth rate, and average dividends per share, earnings per share and book value per share growth rates. The prospective analysis results in a cost of equity ranging from 10.7 to 11.3 percent for UE.

Based upon a 1986 DCF ranging from 10.9 to 12.5 percent, a comparable earnings test ranging from 12.5 to 13 percent, and a prospective analysis ranging from 10.7 to 11.3 percent, Parcell recommends a return on equity ranging from 11 to 12.5 percent. This recommendation is based upon his opinion that the more recent historical data and a forward looking DCF analysis reflects a lower cost of equity than existed in the 1982 to 1983 period.

Company witness Birdsong also performed a DCF analysis. He used the period December, 1984 through June, 1987 to calculate the yield portion of the formula. Birdsong calculated an average dividend yield during the period of 8.62 percent. To calculate the growth rate, he used the average three to five year estimated growth rate projected by Value Line over the same time period. This analysis resulted in a 4.5 percent growth rate. Adding the yield and growth components from the formula results in a 13.12 percent return on equity figure. Birdsong added flotation costs of .36 percent to arrive at a recommendation of a 13.5 percent cost of equity for the Company.

In the Commission's opinion a longer period than used by the Public Counsel and the Staff is more appropriate for the calculation for the yield portion of the DCF formula. However, the Company's calculation is distorted since it includes the period prior to the Callaway rate order. The Company includes the period subsequent to the in service date of the Callaway plant but prior to the rate order. The

Commission is of the opinion that the period subsequent to the rate order which included the Callaway plant in rates is the appropriate time since it recognizes post Callaway conditions. The period after the rate order does not include any uncertainty regarding rate relief with respect to the Callaway plant. Excluding the period prior to the Callaway rate order results in an average dividend yield of 8.26 percent under the Company's calculation.

The Commission further determines that the growth component should be based on an expected growth rate for the future and not an average of expected growth figures. The record reflects that recent growth estimates have decreased to around 3.5 percent. Therefore, a growth rate somewhere between 3.5 percent and 4 percent is more reasonable than the Company's 4.5 percent.

Finally, the Commission is of the opinion that it is inappropriate to adjust for flotation costs, since the Company has no plans to issue common stock during the period the rates arising from this order are likely to be in effect.

Based upon the competent and substantial evidence, and the considerations set forth above, the Commission finds that the Company's authorized return on equity shall be 12.01 percent, resulting in an overall cost of capital of 9.94 percent.

VI. Phase-In Issues

A. Introduction

In the Callaway rate case, the Commission approved a phase-in of the rate increase associated with the inclusion of the Callaway nuclear plant into rate base. The phase-in encompassed the following features: (1) the phase-in was established for an eight-year period; (2) the equity return on Callaway rate base was deferred and recovered in years five through eight; (3) the Callaway-related deferred taxes were amortized over a two-year period; (4) Westinghouse fuel credits were amortized over a two-year period; and (5) a return was allowed on deferred equity equal to the cost of equity found reasonable in the Callaway case (15.62 percent).

Staff contends that the current phase-in balance is accruing an excessive return and that the Company's current rates, effective April 9, 1987, (year three of the phase-in) are excessive. Staff maintains that current rates are more than sufficient to cover the Company's current cost of service and recover the accrued phase-in balance at March 30, 1987, assuming this balance is amortized over a five-year period. Staff's case, assuming a March 30, 1987 balance of phase-in accruals, results in a rate decrease of approximately $31,680,000 from current levels.

Based on the Commission's finding herein set forth in Section V. B. above, the Company's cost of equity is now 12.01 percent in contrast to the 15.62 percent found reasonable in the Callaway rate case. This change in the Company's cost of money requires an adjustment to the phase-in plan. If a just and reasonable rate can support the accrual balance and the current cost of service, the Commission is of the opinion that a return to traditional ratemaking is in the public interest. At a minimum, the continued carrying cost on the deferrals at an excessive return must cease. Based upon the foregoing considerations, the Commission will address the Staff's phase-in adjustments below.

B. Phase-In Credits

Staff proposes that the balance of the accrued phase-in credits as of March 31, 1987, (as offset by the items discussed below) be included in cost of service in this case. Staff proposes that the accumulated balance of phase-in credits be placed in rate base and amortized over a five-year period.

The Company proposes that the phase-in be continued without further modification. However, if the Commission determines that a return to traditional ratemaking is preferred, then Company proposes that the accumulated balance of credits be amortized over a five-year period. The Company opposes any offsetting adjustments to the phase-in accruals and maintains that the cessation of further accumulated credits, the determination of the balance to be amortized and the

beginning of the amortization period should all occur on the effective date of the rates which result from this case. The Company opposes the reduction in the carrying charge from the authorized equity return to the overall rate of return which Staff proposes should be applied to the unamortized portion of the phase-in balance.

In adopting its phase-in plan, the Commission recognized the importance of eliminating any perceived risk or uncertainties regarding the ultimate inclusion in rates of the allowed Callaway costs and deferred equity.

The Commission determines, that to preserve the integrity of the phase-in credits under the phase-in plan, no offset shall be made against the balance. Instead, any adjustments related to deferred taxes and Westinghouse credits shall be made to the cost of service independent of the treatment of phase-in credits. The appropriate treatment for deferred taxes and Westinghouse credits are discussed below.

The Commission further determines that the accrual balance as of December 31, 1987, shall be used for purposes of this case. The estimated balance of $182,185,000 shall be amortized over five years. The unamortized portion shall be placed in rate base and earn the Company's overall cost of capital found reasonable in this case. Although the cost of equity was applied to the deferrals under the phase-in order, this treatment is unique to UE. Commission cases addressing subsequent phase-in plans have applied the overall cost of capital to deferrals during the phase-in period. See: Case No. EO-85-185, Re: Kansas City Power & Light Company, 75 P.U.R.4th 1, 28 Mo. P.S.C. (N.S.) 228 (1986) and Case No. ER-85-265, Re: Arkansas Power & Light Company, 74 P.U.R.4th, 36, 28 Mo. P.S.C. (N.S.) 435 (1986). In the Commission's opinion no justification exists to apply carrying costs in excess of the overall cost of capital for these accruals once the unamortized portion is placed in rate base. Since all costs associated with the Callaway plant will now be reflected in cost of service and no accruals will continue to accumulate in the future, the overall cost of capital is appropriate. These accruals should earn the

overall cost of capital just as all other Company assets included in rate base earn the overall cost of capital.

C. Westinghouse Credits

Staff proposes to reduce the phase-in credit balance by $20,312,000 which represents the balance of accumulated Westinghouse credits at December 31, 1986. The Commission's Callaway rate case order directed that Westinghouse fuel credits be amortized over a two-year period. The phase-in schedule submitted to the Commission by the parties, which formed the basis for the phase-in tariffs, reflected the estimated December, 1984 balance. The Company amortized the amount accumulated as of 1984 over two years (April 1985 through March 1987). However, in addition, the Company amortized the credits which had accumulated at the time of the first reload over the succeeding fuel cycle. Staff contends that the Company's treatment resulted in additional amortization in the amount of $18.4 million in excess of that which was contemplated in the phase-in schedules.

The phase-in schedule does not provide for any amortization of Westinghouse credits beyond year two of the phase-in. Thus, the effect of the Company's amortization of the additional Westinghouse credits not included in the schedule is to thwart the Commission's intention of using those credits to reduce cost of service. Had those additional credits been included in the phase-in schedule, the revenue requirement under the phase-in would have been lower and therefore the phase-in accrual balance would have been lower.

The Company opposes Staff's treatment of the phase-in credits remaining at December 31, 1986. Company contends that it has properly accumulated and amortized the credits over successive fuel loads and proposes that the test year fuel cost reflect the amortization of Westinghouse credits accumulated at the beginning of the last fuel reload. The Company contends that the fuel credits should be amortized over successive fuel cycles. However, the Company proposes that a three-year average of Westinghouse credits be used for the test year amortization.

Since the Commission has determined that the integrity of the phase-in balance should be preserved, no offsets to the balance should be made. However, the Commission determines that the Westinghouse credit balance at December 31, 1986 should be available to reduce cost of service for the test year. Since the credits are associated with nuclear fuel purchases from Westinghouse the Commission believes that it is reasonable to amortize these credits over the fuel cycle occurring as a result of the first fuel reload. Therefore, the 1986 test year shall reflect the amortization of the Westinghouse fuel credits occurring during that portion of the 1986 test year which occurs after the first fuel reload. The unamortized portion should be used as a rate base offset. In the Commission's opinion credits accumulating subsequent to the December 31, 1986 test year shall be amortized over each succeeding fuel cycle.

D. Excess Deferred Taxes

Staff proposes to reduce the phase-in credit balance by $26,813,690 to reflect the balance of unprotected excess deferred taxes at December 31, 1986. $1,219,170 of the balance is a result of the tax rate change from 48 to 46 percent. The remaining balance is a result of the Tax Reform Act of 1986 which changes the tax rate from 46 percent to 34 percent.

The Company opposes an immediate return of these accruals to the ratepayers as a setoff against the phase-in credit balance. The Company proposes to amortize the excess deferred taxes over the remaining life of the property using the average rate assumption method. If the Commission adopts a shorter period, Company recommends no less than a five-year amortization period.

As noted above, the Commission has rejected any setoffs against the phase-in balance. Accordingly, the amortization of the excess deferred taxes shall be considered apart from the phase-in balance.

These deferrals represent taxes collected from ratepayers and intended to be paid as taxes in later years. However, as a result of the tax rate changes, the

deferrals will never become due. In the Commission's opinion, it is equitable to return these deferrals to the ratepayers over the same five year period that the Company will collect the phase-in accrual balance. The Commission sees no merit to making this cost free capital available to the Company over the life of the property. This argument has been accepted in support of normalization accounting where a utility is in need of increased cash flow. At this time, the Company exhibits no cash flow problems.

In addition, the Commission rejects its previous finding that the return of deferred taxes resulting from a tax rate change is inappropriate. In previous cases the Commission has rejected this adjustment because of the risk of a possible adverse Internal Revenue Service ruling and the possibility of losing the benefits of accelerated depreciation and additional tax assessment. See: TR-80-235, Re: United Telephone Company, 24 Mo. P.S.C. (N.S.) 152, 159 (1981). The evidence in this case suggests the amortization of excess deferred taxes does not present any potential violation of the Internal Revenue Code. Therefore, the Commission's previous rationale for excluding this adjustment no longer exists.

In the Commission's opinion these amounts represent deferrals which must be returned to the ratepayer. The question of the period in which the amount should be returned lies within the Commission's sound discretion. The Commission finds that these deferred taxes shall be amortized over five years.

E. CWIP-Related Deferred Taxes

Staff proposes to offset the accrual balance by $9,947,000. This amount represents the deferred tax balance related to the Callaway costs not addressed in the Callaway rate case. The Company opposes this adjustment because of its assertion that the rapid amortization of these taxes are no longer needed as an extraordinary measure associated with the phase-in. Company contends that this amount should be flowed back over the life of the Callaway plant.

In the Commission's opinion, since the additional Callaway costs associated with these deferrals are being included in rate base, it is appropriate to flow these deferrals back to ratepayers over a five-year period. By amortizing the Callaway phase-in deferrals over five years, all costs associated with the initial inclusion of Callaway in rate base will be recovered during the period set for the original phase-in plan. The Commission believes that it is appropriate to amortize the deferred taxes associated with the CWIP portion over the same five-year period since this portion of plant is now being recognized in rate base. This is consistent with the treatment of the Callaway plant and deferred taxes pursuant to the original phase-in plan.

F. Callaway-Related Deferred Taxes

Staff proposes to offset the phase-in accrual by $46,338,000. This amount represents the difference between the amount contained in the phase-in schedule and the amount actually amortized by the Company over the first two years of the phase-in.

As part of the phase-in plan in the Callaway rate case, the Commission ordered that Callaway-related deferred taxes be amortized over a two-year period. The amount contained in the phase-in schedule which served as a basis for the phase-in tariffs was $144,764,000 ($72,382,000 per year). However, the Company amortized $191,102,000 ($95,551 per year) over the first two years of the phase-in. The Company opposes Staff's adjustment on the following grounds: (1) the Company opposes any setoff against the phase-in accruals; (2) the adjustment constitutes retroactive ratemaking; (3) rapid amortization of deferred taxes is no longer needed to address rate shock.

The Commission has accepted the Company's argument that no setoff should be made against the phase-in accruals. Thus, the Commission must consider whether it is appropriate to make an adjustment reflecting the amount of deferred taxes which the Company amortized in excess of that contained in the phase-in schedule.

The Commission approved a two-year rapid amortization of Callaway-related deferred taxes. The Company amortized an amount in excess of $144,764,000, the amount used for the calculation of the phase-in schedule on which the Commission relied when it approved the phase-in rates. Thus, the Company did not have specific authority to amortize the excess amount. Since the revenue requirement contained in the phase-in schedule is a function of the deferred taxes, the revenue requirement would be lower had the phase-in schedule reflected the increased amounts of Callaway-deferred taxes which the Company ultimately amortized, thereby lowering the phase-in accruals which ultimately must be recovered by the Company.

Since the Commission has accepted the arguments in favor of adhering to the 1986 test year, the Commission determines that the portion of the excess Callaway deferred taxes associated with the test year should be recognized. The excess amortization occurred during the two-year period ending March 31, 1987. Therefore, one year of the period coincides with the test year. Accordingly, it is appropriate to recognize the excess deferred tax amortization which was amortized during the test year. This would equal one-half of the two-year balance, approximately $23,169,000. Based on the foregoing, the Commission determines that it is reasonable and appropriate to amortize the test year portion of the excess Callaway deferred taxes over a five-year period.

The Commission finds that any adjustment to the books of the Company associated with these deferred taxes could be reflected in the current year, 1987, a period when Company earnings have been based on its authorized return on equity of 15.62. Thus, any downward pressure in the Company's earnings per share caused by this adjustment should not impair the Company's financial integrity.

VII. Rate Base - Revenue Requirement

The Commission finds that the rate base to be used for purposes of this case shall be the Company's net original cost rate base which is $3,966,761,000.

Applying the overall return found reasonable in this case of 9.94 percent results in a net operating income requirement of $394,296,000. Based on the findings and conclusions herein, the net operating income available is $390,722,000. Applying the tax factor results in a revenue deficiency of $5,603,000. Since the revenue deficiency includes the recognition of all Callaway-related costs, the Commission finds that the accruals on the rate deferrals under the phase-in plan shall end December 31, 1987, the phase-in previously adopted shall end as of the effective date of this Order and the Company shall be authorized to increase revenues by approximately $5,603,000. These calculations are based upon Exhibit 179.

VIII. Rate Design

The Commission in its order issued June 22, 1987, ruled that any consideration of rate design would be limited to the question of how any change in revenue requirement should be spread among the various classes to maintain the existing rate design. As a result of this ruling, the Commission granted Staff's motion to strike certain testimony of UE and Industrial Intervenors.

The only competent and substantial evidence addressing the method of spreading the existing rate design among the various classes is contained in Staff witness Proctor's testimony and in Public Counsel witness Thompson's testimony. Witness Thompson concurs with Dr. Proctor's method of calculating class revenue requirements.

The Commission finds that the revenue requirement found reasonable herein shall be allocated to the various classes using the methods set forth in Staff witness Proctor's testimony (Exhibit 118).

Finally, the Commission determines that the industrial intervenors' motion filed November 17, 1987, requesting an evidentiary hearing on rate design issues should be denied. The motion is untimely pursuant to 4 CSR 240-2.110(22). In addition, the motion is an improper attempt to set aside the Commission's order of June 22, 1987, limiting the scope of these proceedings.

Conclusions

The Missouri Public Service Commission has arrived at the following conclusions:

Union Electric is a public utility subject to the jurisdiction of this Commission pursuant to Chapters 386 and 393, RSMo, 1986. The instant complaints were brought against the Company pursuant to 386.390, RSMo, 1986.

The Commission may consider all facts which in its judgment have any bearing upon a proper determination of the setting of fair and reasonable rates.

Based on the revenue requirement found reasonable herein, the Commission concludes that UE shall file revised tariffs designed to increase gross revenues exclusive of gross receipts and franchise taxes over the current existing phase-in tariffed rates by approximately $5,603,000 on an annual basis. The tariffs shall reflect the rate design found reasonable herein.

It is, therefore,

ORDERED: 1. That pursuant to the findings and conclusions in this Report and Order, the phase-in plan previously adopted by this Commission in Case Nos. EO-85-17 and ER-85-160 shall end and the Company shall file, for approval of this Commission, tariffs designed to increase gross revenues exclusive of gross receipts and franchise taxes over the current effective rates of approximately $5,603,000 on an annual basis.

ORDERED: 2. That the Company shall withdraw the phase-in tariffs which are currently on file with the Commission.

ORDERED: 3. That the tariffs authorized herein shall reflect the rate design found reasonable in this Report and Order.

ORDERED: 4. That the tariffs to be filed pursuant to this Report and Order shall be effective for service rendered on and after December 31, 1987.

ORDERED: 5. That late-filed exhibits 165 through 179 as described in Appendix A attached hereto, be, and they are, hereby received.

ORDERED: 6. That any objections not heretofore ruled upon are overruled and any outstanding motions are denied.

ORDERED: 7. That this Report and Order shall become effective on December 31, 1987.

BY THE COMMISSION

Harvey G. Hubbs
Secretary

(S E A L)

Steinmeier, Chm., Musgrave, Mueller, Hendren and Fischer, CC., Concur and certificy compliance with the provisions of Section 536.080, RSMo 1986.

Dated at Jefferson City, Missouri, this 21st day of December, 1987.

APPENDIX A

LATE-FILED EXHIBITS RECEIVED INTO EVIDENCE

Exhibit 165	Union Electric accounting runs, cover letter of October 23, 1987
Exhibit 166	Public Counsel accounting runs, cover letter of November 2, 1987
Exhibit 167	Staff accounting runs, filed November 18, 1987
Exhibit 168	Letter from Examiner Hogerty dated December 7, 1987, requesting scenarios
Exhibit 169	Letter from Examiner Hogerty dated December 9, 1987, clarifying scenario request
Exhibit 170	Company reconciliation, cover letter dated December 9, 1987, in response to scenario request
Exhibit 171	Company revision to reconciliation, cover letter of December 11, 1987.
Exhibit 172	Staff and Public Counsel Reconciliation filed in response to scenario request, cover letter of December 11, 1987,
Exhibit 173	Reconciliation sponsored jointly by Union Electric, Staff and Public Counsel - Staff cover letter of December 17, 1987.
Exhibit 174	Public Counsel letter dated December 17, 1987, relating to differences shown in Exhibit 173
Exhibit 175	Staff letter dated December 18, 1987, relating to differences shown in Exhibit 173
Exhibit 176	Company letter dated December 18, 1987, relating to differences shown in Exhibit 173
Exhibit 177	Company accounting schedule - December 15, 1987
Exhibit 178	Letter from Examiner Hogerty, dated December 18, 1987, requesting additional scenario
Exhibit 179	Reconciliation in response to request of December 18, 1987 - Staff's cover letter of December 18, 1987