BEFORE THE PUBLIC SERVICE COMMISSION
STATE OF MISSOURI

In the Matter of Union Electric Company, d/b/a	)	
AmerenUE's Tariff to Increase Its Annual	)	**Case No. ER-2011-0028**
Revenues for Electric Service.	)	Tariff No. YE-2011-0116

Staff's Reply Brief

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Staff's Reply Brief

COMES NOW the Staff of the Missouri Public Service Commission, by and through counsel, and for its Initial Brief, states as follows:

INTRODUCTION

In its Reply Brief, Staff responds to the arguments set out in the initial briefs.

ARGUMENT

1. Overview and Policy:

The Commission has considered three general rate cases for major electric utilities this spring and, with the settlement of that of The Empire District Electric Company,[1] the present case is the last of them. All three of these cases have presented issues of prudence related to the addition to rate base of significant new construction. The Commission's treatment of prudence in its *Reports & Orders* in Case Nos. ER-2010-0355 and ER-2010-0356 prompts the undersigned to address that issue in the "Overview and Policy" section of this Reply Brief.

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[1] Case No. ER-2011-0004.

A prudence review is an integral and necessary feature of every Staff audit of utility expenditures; it is not something limited to those occasions when major new construction is admitted to rate base. Staff's duty, on behalf of the Commission, is to scrutinize utility spending to eliminate the unreasonable and the unnecessary, and spending of no benefit to ratepayers. In this regard, spending is necessary if, in its absence, the company's ability to serve its customers would be impaired. Spending is reasonable if the value received is commensurate to the amount spent. Spending is beneficial to ratepayers if a distinct and articulable benefit is conferred on them by the expenditure in question. Nothing in this is particularly difficult or complex.[2]

As the Commission well knows, a presumption of prudence is accorded to the utility.[3] This presumption is really only a matter of convenience – it serves to focus attention on those items that are subject to challenge by one party or another on grounds that are reasonable on their face.[4] By statute, the utility bears the burden of proof on every issue.[5] Neither the Commission nor the courts are authorized to shift that burden to Staff or to any other party. However,

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[2] *See generally* 2 L.S. Goodman, ***The Process of Ratemaking*** 839-883 (PUR: 1998).

[3] ***State ex rel. GS Technologies Operating Co., Inc. v. Public Service Commission,*** 116 S.W.2d 680, (Mo. App., W.D. 2003); ***State ex rel. Associated Natural Gas v. Public Service Commission,*** 954 S.W.2d 520, 528-29 (Mo. App., W.D. 1997).

[4] The cases, and the Commission in its KCPL GMO Report & Order (at p. 75), use the phrase "serious doubt." By **serious**, the cases mean **something to be taken seriously**, not something of especial gravity. In other words, the challenge must pass the "straight face test" to trigger heightened scrutiny. Elsewhere, more helpfully, the challenger's burden is described as "a showing of inefficiency or improvidence." *KCPL GMO Report & Order, supra, quoting* ***In the Matter of Union Electric Company,*** 27 Mo.P.S.C. (N.S.) 183, 193 (1985).

[5] Section 393.150.2, RSMo.

by using the presumption of prudence to shift the burden of going forward onto the challenger, rate case expense and the time of the tribunal are conserved.

The Commission now cites Missouri appellate decisions for the prudence standard, although those appellate courts themselves rely on the very cases cited by the Commission in the decisions under review, and has consequently gotten the standard wrong. The Commission recently said, "[i]n the ***Associated Natural Gas*** case, the Missouri Court of Appeals held that the Staff must provide evidence that the utility's actions caused higher costs than if prudent decisions had been made."[6] The Commission went on to say:

> In other words, Staff or the other parties must satisfy the following two-pronged evidentiary test to support a disallowance: 1) identify the imprudent action based upon industry standards and the circumstances at the time the decision or action was made; and 2) provide proof of the increased costs caused by KCP&L's imprudent decisions. To meet this standard, a party must provide substantive, competent evidence establishing a causal connection or "nexus" between the alleged imprudent action and the costs incurred.[7]

In fact, what the Court of Appeals actually said was:

> ANG is not alone in suggesting that, in order to disallow a utility's recovery of costs from its ratepayers, a regulatory agency must find both that (1) the utility acted imprudently (2) such imprudence resulted in harm to the utility's ratepayers.
>
> * * *
>
> Ultimately, the PSC's standards for the recoverability of ANG's costs arise from the statutory mandate that all charges made by a gas company be just and reasonable. Section 393.130.1. It would be beyond this statutory authority for the PSC to make a

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[6] *KCPL GMO Report & Order, supra.*

[7] *Id.,* 76-77.

> decision on the recoverability of costs, based upon a prudency analysis of gas purchasing practices, without reference to any detrimental impact of those practices on ANG's charges to its customers, such as evidence that the costs which ANG is seeking to pass on to its customers are unjustifiably higher than if different purchasing practices had been employed.[8]

The distinction is important. The two-pronged "nexus" test recently described by the Commission is not an accurate description of the challenger's burden in prudence cases; it is, instead -- exactly as the ***Associated Natural Gas*** Court said – a description of the findings necessary to support a disallowance by the Commission. The challenger's burden before the Commission is merely to show "inefficiency or improvidence," thereby triggering the requirement that the ***utility*** prove-up the propriety of its challenged expenditures. It is the ***utility's*** failure to meet ***its*** burden of proof that should result in Commission findings of excessive costs linked to specific acts of imprudence.[9]

In the present case, the prudence issue arises with Staff's proposed disallowance of some $31 million with respect to the so-called Sioux Scrubbers. Staff has shown that the Company suspended construction for a period of time during the late financial crisis, thereby incurring additional costs; Staff asserts that the suspension of construction operations was "imprudent" in the sense of causing costs that were unnecessary, unreasonable and/or of no benefit to

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[8] ***Associated Natural Gas,*** *supra,* 954 S.W.2d at 529-530.

[9] The Court in ***Associated Natural Gas*** was criticizing the Commission's findings, not Staff's evidence. Staff writes because it is vitally important to the future of cost-of-service regulation in this state that the prudence standard be correctly understood and applied. The test applied by a reviewing court to a Commission disallowance is not the test that the Commission should apply to a challenger's assertion of imprudence.

ratepayers.[10] AmMo's defense is that the suspension was prudent in a larger sense because it saved cash at a time when the availability of cash, and its cost, was uncertain. That may be, but the temporary suspension of an ongoing construction project, and the consequent incurrence of otherwise avoidable costs, is necessarily both "inefficient" and "improvident," and Staff has therefore met the challenger's burden. It is up to AmMo to prove that the spending of each and every one of those $31 million additional dollars was "prudent" in the sense of necessary, reasonable and beneficial to ratepayers. It is for the Commission to then make the findings required by ***Associated Natural Gas;*** perhaps AmMo can show that all of those dollars were prudently spent and perhaps only some, or even none. That is for the Commission to determine as the trier of fact.

2. Storm Costs/Vegetation-Infrastructure Trackers

A. Vegetation-Infrastructure:

Staff has no reply on this issue.

B. Storm Costs:

While Ameren argues that Staff uses "erroneous methodology" in calculating its normalized level of storm costs because Staff has "confused and conflated" the two ratemaking principles of normalization and amortization, the confusion and conflation lies with Ameren Missouri.

Staff is well aware that normalization is the process through which regulators attempt to determine the normal level of an item of expense that

[10] "Prudence" in ratemaking is thus a term of art, but, as Goodman, *op cit.,* explains, it ultimately refers to common sense.

historically fluctuates significantly from year to year.[11] In actuality, Ameren Missouri and Staff have calculated their respective normal levels of storm expense in basically the same way.[12] However, in recognition of Staff's practice of supporting specific recovery for extraordinary storm costs, Staff has appropriately taken the next step in the normalization calculation to remove amounts associated with extraordinary storms previously recognized in Case Nos. ER-2008-0318 and ER-2010-0036. Staff removed these extraordinary costs from its normalization calculation to make the normal level more representative of non-extraordinary storm costs. Staff simply finds it is incongruous to on the one hand consider these storms extraordinary (in the sense that they are afforded specific amortization treatment) while on the other hand reflecting the same costs as an ordinary level of storm expense for normalization. For that reason, Staff has removed them from the calculation of the normalized level of storm costs.[13] Also, since the Company is currently recovering these storm costs through the amortizations established in Case Nos. ER-2008-0318 and ER-2010-0036, recognizing these cost recoveries again by including them in the normalized level is an attempt by the Company to double recover these costs.[14]

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[11] AmMo Initial Brief, p. 110.

[12] Adopting a 47-month average of non-labor related storm costs which begins at the same starting point as Staff, April 1, 2007, through the true-up cut-off date, February 28, 2011.

[13] Staff's Initial Brief, p. 14.

[14] Staff's Initial Brief, p 12-13.

Regarding the issue of amortizations, Ameren Missouri seems to be the confused party on this subject. Staff's Initial Brief and Mr. Cassidy's Surrebuttal both include discussions of the proper purpose and method of calculating an amortization.[15] Put briefly, an amortization is created by comparing the test year level of expense to the normalized level of expense -- if the test year level of costs exceeds the normalized level of expense, an amortization is created to recover the difference over a certain amount of time. As detailed in Staff's Initial Brief, there is no need to establish an amortization since the test year level is less than the normalized level in this case. Ameren Missouri is confusing the issue by attempting to create a new test year, the twelve months ending February 28, 2011.[16] However, the Commission-ordered test year in this case is the twelve months ending March 31, 2010.[17] By attempting to change the test year in this case, Ameren Missouri is explicitly failing to follow the method for determining non-labor storm costs endorsed by the Commission in Case No. ER-2010-0036. While one can certainly understand Ameren Missouri's motivation in seeking an amortization, it simply is not proper here.[18] Furthermore, to include the $8.1 million of storm preparation costs that occurred during the true-up period in the determination of the normalized level and then also to recommend the

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[15] Staff's Initial Brief, pp. 12-15. Ex. 207, John Cassidy Surrebuttal Testimony, ER-2011-0028, pp. 10-11.

[16] Cassidy Surrebuttal, p. 10.

[17] *Id.*

[18] Amortizations can continue to be recovered beyond their expiration date because of the nature of ratemaking, rates cases are seldom timed with the expiration date of an amortization, which can lead to over-recovery. Tr. Vol. 18, p. 339, lines 6-14.

inclusion of an additional amortization between the normalized level and the $8.1 million represents an attempt by the Company to double recover these costs.[19]

Lastly, Ameren Missouri states that, "there is ample evidence that excluding those costs from the average will significantly understate both the amount of normal storm costs Ameren Missouri has incurred in the past and the amount it will likely incur over the future period when rates set in this case will be in effect."[20] This is in interesting statement considering that Ameren Missouri has pontificated at length on the Staff's "confusion" and "conflation," but has failed to cite or direct the Commission's attention to any authority for its understanding of normalization or amortization. Further, Ameren Missouri has failed to include citations to any of its "ample evidence" that purportedly shows that Staff's average understates Ameren Missouri's past and future storm costs.[21] What the record does reflect, however, is that storm costs cannot be predicted, and vary greatly from year to year,[22] that Ameren Missouri has other options in recovering extraordinary storm costs,[23] that Ameren Missouri's costs through the true-up period were covered by the rates in effect at the present time,[24] that Staff has

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[19] Staff's Initial Brief p. 15.

[20] AmMo Initial Brief, p 112-113.

[21] AmMo Initial brief, p. 113.

[22] Cassidy Surrebuttal, Attachment 3.

[23] Tr. Vol. 18, pp. 340-341.

[24] MIEC Initial Brief, pp. 21-22.

consistently supported amortization and recovery of extraordinary storm costs,[25] and that Ameren Missouri is simply asking too much.[26]

In conclusion, the Commission should deny Ameren Missouri's request for an amortization in this case. Further, the Commission should set the base level for storm costs at $4.8 million.

3. Sioux Wet Flue Gas Desulfurization (WFGD) Retrofit Project ("Sioux Scrubbers"):

> Should the Commission allow in rate base $31 million in cost increases ($18 million in construction costs and $13 million in AFUDC) that were incurred as a result of Ameren Missouri's decision to temporarily suspend construction of the Sioux Plant Wet Flue Gas Desulfurization Project due to the Company's concerns about conditions in the financial markets during the period commencing in late 2008 and continuing into early 2009?

Ameren Missouri's Initial Brief on the Sioux scrubbers Project characterizes the Staff as some misguided force, possibly even Satanic, inexplicably frustrating the proper functioning of utility regulation in Missouri. At page 67 of its Initial Brief, Ameren Missouri asserts regarding a 2008 Ameren Missouri ** [redacted] ** proposed financing application, "[a]s a result of Staff's vehement opposition to its request and the immediacy of Ameren Missouri's need to immediately improve its liquidity position, Ameren Missouri abandoned the idea of filing a contested filing case before the Commission." Thus, the Staff is charged with having the power to prevent Ameren Missouri from making a financing filing. At footnote 311 on page 67 of Ameren Missouri's

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[25] Tr. Vol. 18, p. 341, lines 2-11..

[26] Cassidy Surrebuttal, p. 8, ll 12- 16; p. 11, ll. 12-19.

Initial Brief, Ameren Missouri appears to even contend that it is the Staff that promulgates rules. Ameren Missouri states: "Ameren Missouri is unaware of any justification for the **Staff's rule** restricting a long-term debt request to the outstanding short-term debt, particularly in light of a credit crisis where cash is the best form of liquidity."[27]

When, at page 67 of its Initial Brief, Ameren Missouri states that the Staff indicated "vehement opposition" to Ameren Missouri's October 21, 2008, proposed financing application, it does so without mentioning the ** ** parameters and utter lack of other details, all of which so concerned the Staff, as testified to by Mr. Murray. In fact, nowhere in its Initial Brief on the Sioux scrubbers Project does Ameren Missouri mention that the Ameren Missouri proposed financing application that was the subject of its October 21, 2008, conference call with the Staff was to be a ** ** application. Also at page 67 of its Initial Brief, Ameren Missouri leaves the impression, as Mr. Birdsong left in his rebuttal testimony,[28] that based on the Staff's reaction in the October 21, 2008, conference call, Ameren Missouri immediately abandoned a fall 2008 financing filing with the Commission. Staff Exhibit No. 234(HC) comprises Mr. Michael G. O' Bryan's November 7, 2008, "Memorandum To: File," Ameren Missouri draft financing applications, and Ameren Missouri e-mails from October 14, 2008, to November 3, 2008. Staff

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[27] Ameren Missouri Initial Brief, p. 67, n. 311; Citations omitted; Emphasis added.

[28] Ameren Missouri Ex. 109(P), Birdsong Reb., p. 17, ll. 5-13.

Exhibit No. 234(HC) indicates that Ameren Missouri did not immediately decide after the October 21, 2008, conference call with the Staff to abandon a fall 2008 financing filing with the Commission.

At page 61 of its Initial Brief, Ameren Missouri asserts that the "Staff's recommendation to disallow the costs associated with delaying the Sioux Scrubber Project betrays its failure to appreciate the true extent and severity of the financial crisis in late 2008 and early 2009." Ameren Missouri is actually saying that the Staff's unwillingness to agree to Ameren Missouri's October 21, 2008, ** ** proposed financing application "betrays its failure to appreciate the true extent and severity of the financial crisis in late 2008 and early 2009." Ameren Missouri directly says this at page 67 of its Initial Brief in citing Mr. Birdsong's characterization of the Staff's reaction to Ameren Missouri's October 21, 2008, ** ** proposed financing application.[29] Mr. Murray acknowledged in his surrebuttal testimony that there was a financial crisis at the time and related that the very seriousness of it caused the Staff to be concerned whether Ameren Missouri's debt capacity would be used for Ameren's other operations.[30] Mr. Murray also explained that in the past, when utilities' proposed financings have focused on identified Missouri operational needs, the Staff has not opposed such financings.[31]

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[29] Vol. 20, Tr. 5, ll. 9-17.

[30] Staff Ex. 220, Murray Sur., p. 28, ll. 6-10.

[31] *Id.* at 28, ll. 11-15 and p. 29, ll. 1-6.

Ameren Missouri's Initial Brief states at page 64 that ** [redacted] ** By November 20, 2008, the date of Mr. Thomas R. Voss' appearance before the Commission in Case No. ER-2008-0318, Ameren Missouri had abandoned its intention to file its ** [redacted] ** proposed financing application. It should be noted that Mr. Voss, who appeared before the Commission as AmerenUE's President and Chief Executive Officer on November 20, 2008, did not raise any concerns regarding Ameren Missouri's liquidity in his testimony before the Commission on that date.[32]

At page 64, Ameren Missouri's Initial Brief notes Mr. Birdsong's testimony that Ameren Missouri could not take chances whether it would run out of the cash needed to deliver utility service, but at page 68 there is the un-sourced statement that Ameren Missouri "did know the result of an extended crisis would be an inability to provide service to its customers." The subtlety of the fact that Ameren Missouri had a $251 million permanent rate increase case, Case No. ER-2008-0318, pending at the time of the late 2008 – early 2009 financial crisis / Sioux scrubbers Project slowdown should not be lost. The Commission issued its Report and Order on January 27, 2009, with a February 6, 2009, effective date in which it authorized Ameren Missouri a permanent increase in rates of

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[32] Staff Ex. 213, Grissum Sur., p. 12, ll. 1-4.

approximately $163 million, a 10.76% return on equity, and the use of a fuel adjustment clause, among other things.[33]

Also, the possibility of interim / emergency rate relief in a financial crisis for a utility is possible as Mr. Voss testified in Case No. ER-2008-0318.[34] In ***State ex rel. Fischer v. Public Service Commission*,**[35] the Western District Court of Appeals, in discussing interim rate increases, noted the emergency criteria:

> . . . *the Commission's authority to grant an interim rate increase is* necessarily implied from the statutory authority granted to enable it *to deal with a company in which immediate rate relief is required to maintain the economic life of the company so that it might continue to serve the public***.**

The standard for interim rate relief was set forth in, among other cases, ***In re Missouri Public Service Company***.[36] To be eligible, a utility company must show that: (1) it needs the additional funds immediately, (2) that the need cannot be postponed, and (3) that no other alternatives exist to meet the need but rate relief. "Although the Commission has, on occasion, granted interim rate relief in a nonemergency situation, those instances are few and in response to particular ***pressing*** circumstances" (emphasis added).[37]

In recent years, the Commission reaffirmed its allegiance to the emergency standard in its March 8, 2001, order rejecting Empire's interim filing of

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[33] ***In re Union Electric Company doing business as AmerenUE,*** Case No. ER-2008-0318 (***Report & Order,*** 2009) pp. 5, 32, 76.

[34] *Id*. at 10, ln. 26 – p. 11, ln. 41.

[35] 670 S.W.2d 24, 26 (Mo. App., W.D. 1984).

[36] Case No. 18,502, 20 Mo.P.S.C. (N.S.) 244 (1975).

[37] ***In re Missouri Power & Light Co.,*** Case Nos. GR-81-355 and ER-81-356 (1981).

February 16, 2001, Case No. ER-2001-452, which was made in connection with a permanent rate case, Case No. ER-2001-299. The Commission stated, "[t]he proper application of the standard is that a utility must need an interim rate increase in order to meet the emergency or near emergency it faces.FN 2"[38] Footnote 2 of that ***Order Rejecting Tariffs And Granting Motion To Dismiss*** explains as follows:

> As Empire notes in its pleadings, the Commission did partially develop a "good cause" standard for interim relief in *In Re The Empire District Electric Company*, 6 MoPSC 3rd 17 (Case No. ER-97-82). However, in that case the Commission based its denial of Empire's request on its conclusion that: "There is no showing by the Company [Empire] that its financial integrity will be threatened or that its ability to render safe and adequate service will be jeopardized if this request is not granted." The differences, if any, between this good cause standard and the historically applied emergency or near emergency standard were not clearly annunciated, and the Commission now returns to its historic emergency or near emergency standard.

At the bottom of page 62 and the top of page 63 of its Initial Brief, Ameren Missouri cites its negative free cash flow as support for the Sioux Scrubbers Project slow-down. The Commission's *Report & Order Regarding Interim Rates* issued on January 13, 2010, in Ameren Missouri's last permanent rate increase case, Case No. ER-2010-0036, states at page 8 that some amount of negative free cash flow for an electric utility like Ameren Missouri is normal:

> Second, while AmerenUE is currently experiencing a large negative cash flow, some amount of negative cash flow for an electric utility such as AmerenUE is normal. Indeed, AmerenUE has not had a positive cash flow since 2000. Cash flows did not turn sharply negative until 2005 when AmerenUE sharply increased

[38] ***In re The Empire District Electric Co.,*** 10 Mo.P.S.C.3rd 124, 126 (2001).

> its capital expenditures. Thus, while AmerenUE's concern about negative cash flows certainly explains the company's desire for an interim rate increase, the evidence does not demonstrate that any systemic regulatory lag problem in Missouri is causing AmerenUE's negative cash flow.
>
> Despite AmerenUE's current negative cash flow of approximately $150 million for 2009, the company's bond ratings have remained stable. Currently the company maintains an investment grade bond rating of BBB, A3, and A from Standard & Poor's, Moody's and Fitch respectively, and that bond rating outlook is stable. Furthermore, Standard & Poor's has continued to rate AmerenUE as having an excellent business risk profile.

The Commission noted at page 6 of its *Report & Order Regarding Interim Rates* that Ameren Missouri experienced approximately $1.6 billion negative free cash flow between January 1, 2007 and June 30, 2009.

Ameren Missouri notes in its Initial Brief at pages 74 and 76 that the replacement of the flakeglass lining in the interior of the Sioux scrubber absorber units with Stebbins tile was an "unanticipated in November 2008" / "unexpected" benefit of the slowdown. It was not any part of the analysis for the slowdown. Although a request from the Staff did not prompt Ameren Missouri to calculate the savings from the Stebbins tile,[39] a request at the hearing from Commissioner Kenney caused Ameren Missouri to project the savings from the Stebbins tile, based on Ameren Missouri's assumptions, and file those projected savings on May 6, 2011, as a late-filed exhibit:

> **COMMISSIONER KENNEY**: Have you quantified the savings from having switched to the Stebbins tile, if there was any savings?

[39] Vol. 19. Tr. 565, l. 25 – Tr. 566, l. 3.

MR. BIRK: Well, what we believe was -- the savings will be in the -- in the longer-term maintenance and in the better operation of the unit. There's less temperature restrictions with the tile in the way you can move the unit around, temperature restrictions inside the scrubber. Plus, our understanding with the coating was that you would expect about a ten-year life. Well, the tile itself, you know, life of that is the life of the scrubber, which is 30 years or longer, so while we haven't specifically quantified in dollars, the savings were in better operation in maintenance, basically.

COMMISSIONER KENNEY: Is it possible to quantify that savings in dollars?

MR. BIRK: That would be something **we would have to go back and look at and try and make assumptions on**, you know, what it would take -- you know, what maintenance would be required on the other coating, things like that.[40]

* * * * *

COMMISSIONER KENNEY: Do you know how much, or if -- are you able to quantify any savings that will be realized as a result of replacing the old tile with the Stebbins tile?

MR. BIRDSONG: I think that with utilizing Mr. Birk's staff, **we could come up with an estimate** for that, but that calculation has not been calculated and **we'd have to make some assumptions** in coming up with such an estimate, but I think we can do that.

* * * * *

JUDGE WOODRUFF: Commissioner, what we'll do on that, then, if you like, we'll reserve an exhibit number and ask them to file it within, say, a week.

COMMISSIONER KENNEY: That's fine.

MR. LOWERY: Can we have till the end of next week?

JUDGE WOODRUFF: That's fine.

[40] Vol. 19, Tr. 447, l. 21 – Tr. 448, l.18.

MR. LOWERY: And we'll discuss it with Mr. Birk and his staff to see what could be done it. **Assumptions would have to be made**, of course.

JUDGE WOODRUFF: That would be No. 155 as a late-filed exhibit.

COMMISSIONER KENNEY: Thank you.

JUDGE WOODRUFF: And end of next week would be May 6.[41]

Ameren Missouri at pages 72-73 of its Initial Brief states that Ms. Grissum faulted Ameren Missouri at the evidentiary hearing for not providing her with a liquidity analysis to support its decision to delay the Sioux Scrubbers Project, which Ameren Missouri states she did not tell Ameren Missouri she needed until six days before the evidentiary hearing. Staff Data Request No. 139, which is Ameren Missouri Exhibit No. 156, asks among other things respecting Ameren Missouri's decision to delay the Sioux WFGD Project, "[i]nclude copies of any scenario or economic analyses performed by Ameren, Ameren Services (AMS), AmerenUE (UEC), Project Operations Services (POS) or other affiliated Company." The Ameren Missouri response is dated October 29, 2010, and no liquidity or other economic analysis was provided by Ameren Missouri.[42] Ms. Grissum answered at the evidentiary hearing that she considered the liquidity study, which was provided by Ameren Missouri in response to a subsequent Staff Data Request in the 440 series, should have been provided in response to Staff Data Request No. 139.[43] Staff Data Request No. 442, asked by David Murray,

[41] Vol. 19, Tr. 509, ll. 15-24; Tr. 510, ll. 5-20.

[42] *Id.* at Tr. 639, ll. 15-20.

[43] *Id.* at Tr. 641, ll. 4-13.

Ameren Missouri Exhibit No. 152, was responded to by Ameren Missouri on April 14, 2011, and Staff Data Request No. 443, asked by David Murray, Staff Exhibit No. 234(HC), was responded to by Ameren Missouri on April 13, 2011. The Staff would note certain of Commissioner Kenney's questions to Ms. Grissum and her responses:

> **COMMISSIONER KENNEY**: And then you did not do your own independent liquidity analysis, because you were expecting that Ameren would have done such an analysis in response to DR 139?
>
> **MS. GRISSUM**: Yes. In DR 139, I specifically requested scenario analysis and economic analysis that supported their decision to delay the Sioux project.
>
> **COMMISSIONER KENNEY**: What would you have wanted that liquidity analysis to have yielded to have satisfied you that it was a prudent decision?
>
> **MS. GRISSUM**: Well, I understand that the liquidity is the reason given by the Company, but in justifying the decision to slow it down, what I would have looked at, from a financial background, is I would have looked at some -- applying some type of capital budgeting techniques that would have compared the estimated costs that they were going to reduce and see what it would cost them to go out and borrow money to cover those shortfalls and at what interest rate and to see what the cost impact of that scenario would be versus the scenario simply slowing down the project and incurring either the 53.8 that they originally estimated or the ultimate 31,000,000 that they actually incurred.
>
> And then I would have looked to see which decision would have been more cost beneficial and provided the least impact to Ameren.[44]

At pages 63 and 68, footnote 314, of Ameren Missouri's Initial Brief, Ameren Missouri mentions the $1.15 billion credit facility ($500 million of which

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[44] *Id.* at Tr. 633, l. 13 – Tr. 634, l. 15.

was directly available to Ameren Missouri), but that one third of the credit commitment was with banks which Mr. Birdsong testified were "**rumored**" to be on the brink of insolvency.[45]

Regardless of whether the Commission accepts any of the Staff's proposed Sioux WFGD Retrofit Project adjustment, Ameren Missouri misstates the law when its Initial Brief: (a) basically asserts at the top of page 77 that un-rebutted evidence is credible evidence, and (b) declares at page 73 that "[b]ecause Ms. Grissum has failed to offer evidence to create this serious doubt [of prudence], Ameren Missouri's decision retains its presumption of prudence, and this Commission has no basis to disallow the costs associated with the delay of the project." Contrary to Ameren Missouri's position, testimony does not need to be refuted in order for the Commission to lawfully disbelieve it.[46] The Missouri Supreme Court has clearly stated that the Commission determines the weight of evidence presented to it and may disregard evidence which in its judgment is not credible, even though there is no countervailing evidence to dispute or contradict it:

> Rice objects to the findings of the commission because they ignore his evidence. **He contends since there was no other evidence adduced which contradicted his figures and calculations, or even disputed them, that the commission is bound to accept them as true. Accordingly he contends his evidence is the only substantial evidence in the record. In asserting his contention he overlooks that on cross examination his evidence was discredited to such an extent**

[45] Emphasis added.

[46] ***State ex rel. Rice v. Public Serv. Comm'n*,** 359 Mo. 109, 116-17, 220 S.W.2d 61, 65 (Mo. banc 1949).

> **that the commission held it not entitled to credence. And certainly if evidence is not credible, it does not meet the required test of being substantial. An appellate court as a matter of law passes upon the matter of substance and not of credibility.** In other words an appellate court may say that particular evidence is substantial if the triers of the facts believed it to be true.
>
> Whenever an investigation is conducted by the commission it is required under the statute to make a report in writing which shall state its conclusions and its decision or order. Thus it must find and determine the facts. And in doing so **the commission determines the weight of evidence presented to it. It may disregard evidence which in its judgment is not credible, even though there is no countervailing evidence to dispute or contradict it. The rule is established in this State that the triers of fact under their duty to weigh the evidence may disbelieve evidence although it is uncontradicted and unimpeached.**[47]

Elsewhere, the Missouri Supreme Court has stated that "[n]o one questions the rule that an administrative agency in determining a question of fact may pass upon the credibility of witnesses and where a claimant has the burden of proof may decide a claim solely upon a finding of lack of credibility of uncontradicted and unimpeached testimony offered in support of the claim.[48]

In a more recent case respecting the Commission, the Western District Court of Appeals stated that in evaluating expert testimony the Commission may adopt or reject any or all of any witness' testimony:

> Not only can the Commission select its methodology in determining rates and make pragmatic adjustments called for by particular circumstances, but it also may adopt or reject any or all of

[47] *Id.* (internal citations eliminated; emphasis added).

[48] ***Koplar v. State Tax Comm'n***, 321 S.W.2d 686, 694 (Mo. 1959) (citations omitted; the Court relied in part upon ***Rice,*** *supra*).

> any witnesses' testimony. Evaluation of expert testimony was for the Commission.[49]

The Court stated in 1985 that "[t]he Commission as the trier of fact was free to choose between conflicting testimony."[50]

Evidentiary determinations by the Commission are favored by a strong presumption of validity, which extends to determinations based on expert opinion.[51] The opinion of a qualified expert may amount to competent and substantial evidence.[52] It is up to the Commission to choose between the conflicting evidence of expert witnesses, if the testimony was properly presented to the Commission.

4. Energy Efficiency/Demand Side Management (DSM):

A. Is Ameren Missouri in compliance with the Missouri Energy Efficiency Investment Act (MEEIA) regardless of whether or not proposed rules under the law are effective?

(1) What DSM programs should Ameren Missouri continue and/or implement, and at what annual expenditure level; and

(2) Should Ameren Missouri continue to ramp up its demand side management programs to pursue all cost-effective demand side savings?

B. Does Ameren Missouri's request for demand-side management programs' cost recovery in this case comply with MEEIA requirements?

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[49] ***State ex rel. Associated Natural Gas Co. v. Public Serv. Comm'n***, 706 S.W.2d 870, 880 (Mo. App., W.D. 1985) (citations omitted); *see* ***State ex rel. Associated Natural Gas Co. v. Public Serv. Comm'n***, 37 S.W.3d 287, 294 (Mo. App., W.D. 2000).

[50] *Id.,* at 882.

[51] ***State ex rel. Missouri Pub. Serv. Co. v. Pierce***, 604 S.W.2d 623, 625 (Mo. App. 1980).

[52] ***State ex rel. Associated Natural Gas Co. v. Public Serv. Comm'n***, 37 S.W.3d 287, 294 (Mo. App., W.D. 2000), *citing* 2 Am.Jur.2d., Adm.Law § 395, p. 201 (1962).

(1) Should the Commission approve a cost recovery mechanism for Ameren Missouri DSM programs as part of this case? If so,

(a) Over what period should DSM program costs incurred after December 31, 2010, be amortized?

(b) Should the mechanism include an adjustment to kWh billing determinants?

(c) How much should the Commission reduce the billing determinants? and

(d) If billing units are adjusted for demand side savings, how should the NBFC rates be calculated?

C. Should a portion of the low income weatherization program funds be utilized to engage an independent third party to evaluate the program?

For brevity, the Staff will ask the Commission refer back to its initial brief.[53] The Staff will only restate its recommendations to the Commission and address certain arguments made by AmMo concerning this issue.

The Staff makes the following recommendations to the Commission on Demand-Side Management (DSM):

1. That the Commission order AmMo to continue its current DSM programs at an annual spending level no less than its low risk DSM preferred resource plan filed in File No. EO-2011-0271. The Commission's Order for AmMo to continue its DSM programs should not equate to the Commission's approval of programs under MEEIA, because the Company did not request, nor did the Staff

[53] Staff's Initial Brief, pp. 44-53.

evaluate, such a request for approval of DSM programs through a MEEIA application in this case;

2. That the Commission not change AmMo's current DSM cost recovery mechanism from its current six-year amortization to a three-year amortization, because approval of AmMo's request will not create the necessary financial incentives for the Company to comply with the MEEIA;
3. That the Commission not approve either of the mechanisms for recovery of lost revenue proposed by AmMo in the direct, rebuttal or surrebuttal testimony of Mr. Davis, because: a) these mechanisms proposed by AmMo are lost-revenue-recovery mechanisms, which are inconsistent with the provisions for a utility lost-revenue component of a demand-side programs investment mechanism (DSIM) included within the Commission's now-effective MEEIA rules; b) approval of either mechanism will not create the necessary financial incentives for AmMo to comply with MEEIA; c) neither mechanism removes the Company's throughput incentive; and d) the Company has not requested Commission approval of its demand-side programs under MEEIA, a statutory condition for receiving a Commission-approved DSIM; and
4. That the Commission encourage AmMo to pursue a comprehensive strategy consistent with MEEIA or with the Commission's MEEIA rules that aligns the Company's financial incentives with helping its

> customers use energy more efficiently. The Company should focus its attention on working with its stakeholders to achieve by January 1, 2012, the filing of applications for approval of its realistic achievable potential (RAP) demand-side programs described in Case No. EO-2011-0271, and for approval of a DSIM under the effective MEEIA rules.[54]

Program Approval:

It is important for the Commission to realize that while AmMo may be a "victim of its own success," the Company is also a victim of its own failures. The Company states, "[u]nfortunately, the current regulatory framework makes Ameren Missouri a victim of its own success in that the successful implementation of energy efficiency causes the Company financial harm."[55] However, the Company chose not to file a MEEIA application in this case. If the Company wants to characterize Staff's insistence on compliance with the statute as a "roadblock," then so be it. AmMo is using its failure to file a MEEIA application to hold the Commission captive and say the Company will not invest in energy efficiency unless the Commission grants the specific recovery it seeks, despite its failure to meet the requirements of the statute, let alone the Commission's rules. It is improper for AmMo to thrust its failures at the Commission to receive the late proposed mechanisms the Company states it requires to continue to invest in energy efficiency; requirements that the

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[54] Surrebuttal Testimony of John A. Rogers, Ex. 222, p. 2, l. 6 – p. 3, l. 10; p. 6, ll. 36-39.

[55] Initial Post-Hearing Brief of Ameren Missouri, p. 93.

Company is statutorily required to meet regardless of whether rules were in place at the time the Company filed its case.[56]

Additionally, AmMo's brief states that the "Staff recommends that the Commission do nothing in this case and, rather, that Ameren Missouri be required to make a separate filing under the new MEEIA rules."[57] This is an inaccurate characterization of the Staff's recommendation for the Company. Without an application meeting the requirements of the MEEIA statute and/or MEEIA rules from the Company, there is very little the Staff can do in this case. MEEIA and the MEEIA rules are clear on this point.

The Company attempts to differentiate itself from the Commission's order on this issue in the Kansas City Power & Light Company (KCP&L) and KCP&L – Greater Missouri Operations Company (GMO) rate case. The Commission's Order in that case states:

> The Commission concludes that the continuance of the DSM programs is in the public interest as shown by the customer participation and clear policies of this state to encourage DSM programs. In the absence of a clear proposal for a cost recovery mechanism and during the gap between the end of the true-up for this case and the implementation of a program under MEEIA, the Commission concludes that the Companies should continue to fund and promote or implement, the DSM programs in the 2005 Agreement (KCP&L only), and in its last adopted preferred resource plan (both KCP&L and GMO).[58]

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[56] Missouri Energy Efficiency Investment Act (MEEIA), § 393.1075.4 RSMo (Supp. 2010).

[57] Initial Post-Hearing Brief of Ameren Missouri, p. 101.

[58] *Id.* at 100; ER-2010-0355, *Report and Order,* p. 91.

AmMo argues in its brief that "KCPL did not request treatment different than what the Commission approved. Ameren Missouri has been very clear in identifying the problems it needs the Commission to address and the mechanism it requests to resolve those problems."[59] The Staff adamantly disagrees with this statement.

Proposing a mechanism during rebuttal, ignoring its impacts on other aspects of the case, and briefly analyzing it in surrebuttal does not, to Staff, amount to a clear proposal. The Company's surrebuttal proposal allowed the Staff two weeks, compared to the approximately nine months available for review, had the Company filed the proposal in its direct case. The Staff had to prepare supplemental testimony during the start of the evidentiary hearing due to the Company's late timing of the proposal. The filing of a MEEIA application would allow a detailed and focused analysis over a period of 120 days[60] for any Company programs, proposals of cost recovery for those programs, incentives and lost revenue proposals.

AmMo also argues that its proposal "…is the only constructive proposal in the case. Rather than waiting and hoping that the next filing will present a solution, the Commission should act now."[61] It may be true that the Company's proposal is the only one in the case, but that is because ***only*** the Company is

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[59] Initial Post-Hearing Brief of Ameren Missouri, p. 100.

[60] Rule 4 CSR 240-20.094(3).

[61] Initial Post-Hearing Brief of Ameren Missouri, p.102.

responsible for proposing any recovery of program costs, incentives and lost revenues.

The Company asks the Commission to act now, but on what information? Case law requires that the Commission have substantial and competent evidence in the record as a base for its decision. AmMo has not filed a MEEIA application that would allow the Commission to consider granting the lost revenue recovery mechanism the Company seeks. The Staff recommends that before the Commission allows guaranteed recovery of presumed lost revenue equal to approximately 13.9 percent of the non-fuel rate increase requested in this case, the Company be required to file a MEEIA application with the Commission.

Cost Effectiveness of Programs:

MEEIA provides "[t]he commission shall permit electric corporations to implement commission-approved demand-side programs proposed pursuant to this section with a goal of achieving all cost-effective demand-side savings."[62] AmMo states, "[o]ther parties appear to believe all cost-effective requires expenditures geared toward achieving the Realistic Achievable Potential (RAP) levels of MWh savings. The fatal flaw in this belief is that it overlooks the immediate and negative impact of achieving the savings upon the utility's revenues, the throughput disincentive."[63] AmMo is trying to separate out the

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[62] Section 393.1075.4 RSMo (Supp. 2010).

[63] Initial Post-Hearing Brief of Ameren Missouri, p. 102.

analysis of "cost effective" for the customer and for the Company, which is improper for this analysis.

While MEEIA requires a party to conduct a total resource test (TRC) for DSM programs, the TRC does not provide the full analysis to determine whether a program is cost effective. Also, MEEIA does not require that the TRC be the only cost-effectiveness test.[64] The Commission's rules recognize that a more detailed determination of cost-effectiveness comes from the Company's analysis conducted to meet the Chapter 22 Electric Utility Resource Planning filing requirements.[65] That analysis requires the evaluation of demand-side and supply-side resources on an equivalent basis over a twenty-year horizon to determine the risk-adjusted present value of long-term utility costs for each candidate resource plan.[66] According to AmMo's February 2011 Chapter 22 compliance filing, demand-side resources are clearly the lowest cost for the Company over the next twenty-nine years, when compared to any of the alternative supply-side resources.[67]

Putting aside the argument of what "cost effective" means under the statute, the Company can resolve the presumed "flaw" it points out by submitting a MEEIA application for the Commission's review and approval. The Staff recommends that the Commission order AmMo to continue its current DSM

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[64] Section 393.1075.4 RSMo (Supp. 2010).

[65] Rule 4 CSR 240-20.094 (3)(A)3.

[66] Rule 4 CSR 240-20.094 (3)(A)3.

[67] Surrebuttal Testimony of John A. Rogers, Ex. 222, p. 9, ll. 10-17.

programs at an annual spending level no less than its low-risk DSM preferred resource plan filed in Case No. EO-2011-0271, and allow Ameren Missouri to recover its DSM cost through its current cost recovery mechanism until Ameren Missouri makes a complete filing under MEEIA and the Commission approves a cost-recovery mechanism requested through the process defined by the MEEIA rules.

Billing Unit Adjustment Mechanism:

Regarding the kWh billing unit adjustment mechanism, AmMo states in its brief:

> The Company proposed a billing unit adjustment mechanism designed to address the same throughput disincentive problem but in a way that does not conflict with the Commission's definition of lost revenues from ever occurring in the first place, rather than seeking recovery of them after they take place. This is a significant factual distinction.[68]

The Company's argument is illogical because it removes the post review of DSM programs expense, a vital part of MEEIA's analysis to insure the program was prudent and successful. No matter what AmMo decides to call the mechanism, it remains a lost-revenue-recovery mechanism because it "seeks to recover fixed costs that the utility would normally expect to recover through the sale of energy absent the implementation of energy efficiency programs."[69] As

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[68] Initial Post-Hearing Brief of Ameren Missouri, p. 98.

[69] Tr. Vol. 26, p. 1878, ll. 5-9; Supplemental Testimony of John A. Rogers, Ex. 246, p. 2, ll. 25-27.

stated by the Missouri Energy Group, the Company's kWh billing adjustment proposal is nothing more than a thinl-veiled lost-revenue-recovery mechanism[70].

MEEIA states, "[r]ecovery for such programs shall not be permitted unless the programs are approved by the commission, result in energy or demand savings and are beneficial to all customers in the customer class in which the programs are proposed, regardless of whether the programs are utilized by all customers."[71] Further, MEEIA Rule 4 CSR 240-20.093 allows the utility to recover lost revenue **only when and to the extent that energy efficiency programs cause a drop in sales below the levels used to set the electricity prices**. In contrast, Ameren Missouri's proposal for a billing unit adjustment does not take into account growth in usage and occurs before there is an actual drop in usage due to the energy-efficiency programs below the level used to set the electricity prices. The Commission should not approve AmMo's proposal for a billing unit adjustment mechanism, since it is inconsistent with the MEEIA statute and the Commission's MEEIA rules and would allow Ameren Missouri to recover forecasted lost revenue resulting from demand-side savings, even if the Company's retail energy sales are growing.[72]

Again, the Company attempts to differentiate itself from the Commission's order on this issue in the KCP&L and KCP&L – GMO rate case as quoted above. And, as pointed out by AmMo, no party has testified that the kWh billing unit

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[70] Initial Post-Hearing Brief of The Missouri Energy Group, p. 3.

[71] Section 393.1075.4 RSMo (Supp. 2010).

[72] Supplemental Testimony of John A. Rogers, Ex. 246, p. 3, l. 27 – p. 4, l. 2.

adjustment mechanism "couldn't work."[73] However, "couldn't work" and "should approve" are two very different things. The Staff recommends that before the Commission allows guaranteed recovery of presumed lost revenue for approximately 13.9 percent of the non-fuel amount of revenue requirement increase requested in this case, the Company must file a MEEIA application with a thorough analysis that the Staff and other parties can fully evaluate.

Rate Design Modification:

MEEIA provides that "[p]rior to approving a rate design modification associated with demand-side cost recovery, the commission shall conclude a docket studying the effects thereof and promulgate an appropriate rule."[74] There is a workshop docket, File No. EW-2011-0372, currently open before the Commission. The Staff's witness testified at hearing that AmMo's kWh billing unit adjustment might be a form of rate design modification.[75] The Company argues that this is just an "illustration of the unwillingness of Staff to work with utilities to find a constructive resolution and of its apparent desire to simply throw up every conceivable roadblock…"[76] However, the Staff is following the mandate of the statute. Before the Commission can approve the kWh billing unit adjustment proposal, it must study rate design modification for DSM programs and promulgate appropriate rules.

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[73] Initial Post-Hearing Brief of Ameren Missouri, p. 100.

[74] Section 393.1075.5 RSMo (Supp. 2010).

[75] Tr. Vol. 26, p. 2019, ll. 24-25 – p. 2020, ll. 1-6.

[76] Initial Post-Hearing Brief of Ameren Missouri, p. 104-105.

Conclusion:

The constantly-repeated refrain in Staff's arguments on these related issues is that Ameren Missouri must file a MEEIA application. Staff urges the Commission to require Ameren to do what the law requires. Reward desired behavior and do not reward non-compliance.

5. Taum Sauk:

Staff has no reply on this issue.

6. Municipal Lighting:

Staff has no reply on this issue.

7. Cost of Capital:

The largest single revenue requirement issue before the Commission in this case is the cost of capital and there is only a single decision point under that heading: what return on equity ("ROE") will the Commission allow to AmMo?

It's a Two-Step Process:

In its Initial Brief, Staff presented a review of the ratemaking jurisprudence of the United States Supreme Court in order to clarify the analytical process required by the constitutional principles that necessarily must guide the Commission in its difficult task of setting AmMo's ROE.[77] The Court focuses on the identification of the Lowest Reasonable Rate, which is just above the point of confiscation and which is the floor of the "zone of reasonableness" within which the Commission has discretion to set the ROE. Somewhere above that floor is

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[77] *Staff's Initial Brief* (HC & NP), pp. 57-62.

the top of the zone of discretion, which is the point at which the ROE becomes so excessive that the Due Process rights of the ratepayers are violated.[78] The Commission's focus on the average of recent allowed returns and its use of an analytical tool centered on that average, the so-called "Zone of Reasonableness,"[79] has deflected its attention away from the identification of the Lowest Reasonable Rate. The proper starting point is not the middle, but the bottom.[80]

Identifying the Lowest Reasonable Rate must be the first step in the Commission's determination of an appropriate ROE because the ratepayers are presumptively entitled to an ROE at that point and no higher.[81] While it is true that the Lowest Reasonable Rate is the bottom of a range within which the Commission has discretion to set the ROE, it is also true that an unexplained exercise of discretion, not founded on substantial and competent evidence of record, is arbitrary and capricious by definition. The Commission may set AmMo's ROE *higher* than the Lowest Reasonable Rate only in order to

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[78] Implicit in the requirement that rates be "just and reasonable" is the notion that they be no higher than necessary to cover the cost of providing the service, keeping utility assets in proper repair and allowing a reasonable opportunity to earn a profit to the shareholders. *See* ***In the Matter of KCPL Greater Missouri Operations Company,*** Case No. ER-2010-0356 *(****Report & Order,*** issued May 4, 2011) pp. 15-17.

[79] The phrase "zone of reasonableness," without capitalization, refers to the area of rate-setting discretion described by the United States Supreme Court; when capitalized, the phrase refers to the analytical tool used by this Commission.

[80] Emphatically, this is not to say that the benchmarks provided by other allowed ROEs are not analytically useful. They are.

[81] AmMo admits in its *Initial Brief,* "[r]atepayers are entitled to rates that are no higher than necessary to reasonably compensate investors and attract future investment." (p. 9) By definition, that is the Lowest Reasonable Rate, the lowest point where the principles of the Commensurate Return and of Capital Attraction are satisfied. J.C. Bonbright *et al.,* ***Principles of Public Utility Rates*** 315-16 (PUR: 1988).

accomplish relevant regulatory purposes, based on evidentiary determinations described in its Findings of Fact.[82]

Thus, the Commission faces two questions in setting AmMo's ROE: First, what is the Lowest Reasonable Rate? Second, does the record support an ROE higher than the Lowest Reasonable Rate?

What is the Lowest Reasonable Rate?

Four expert financial analysts testified in this case. Their announced purpose was to identify the market-required return, a concept not discussed by the Supreme Court. It is an investment concept, not a legal one. As AmMo's expert witness, Robert Hevert, put it: "When we look at the cost of equity for a company such as Ameren, what we're trying to do is estimate the return required by all equity investors";[83] or, as Mr. Gorman put it, "[t]he required return . . . is your assessment of what would be an appropriate return for assuming the risk of that asset."[84] A textbook explains it this way:

> When an investor makes funds available to a firm, that investor is foregoing the option of using those funds for some other purpose (either current consumption or another investment). The investor is also putting his funds at some risk. Together, these conditions define the investor's *opportunity cost.* In exchange for undertaking this risk, the investor will expect to earn a return on his funds that is commensurate with that opportunity cost.[85]

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[82] ***In re Permian Basin Area Rate Cases,*** 390 U.S. 747, 797-798, 88 S.Ct. 1344, 1376, 20 L.Ed.2d 312, ___ (1968); ***Federal Power Commission v. Natural Gas Pipeline of America,*** 315 U.S. 575, 585-586, 62 S.Ct. 736, 742-743, 86 L.Ed. 1037, ___ (1942).

[83] Tr. 22:1128; *cf.* Gorman, Tr. 22:1247: "I am charged with providing what I believe to be at least a reasonable estimate of what the current investor required return is[.]"

[84] Tr. 22:1226.

[85] L.R. Giacchino & J.A. Lesser, ***Principles of Public Utility Corporate Finance*** (PUR: 2011), p. 141 (emphasis in the original); *and see* ***Verizon Communications, Inc. v. F.C.C.,*** 535

In its Initial Brief, Staff pointed out that the market-required return described by the expert witnesses is essentially the same thing as the Lowest Reasonable Rate discussed by the Supreme Court.[86]

Staff has argued, and now repeats the argument, that only Staff expert witness David Murray has accurately testified to the Lowest Reasonable Rate. The other three experts have instead, under the guise of identifying the market-required return, testified to their clients' desired allowed ROE.[87] For AmMo, the desired allowed ROE is somewhere above the average of recently allowed ROEs

TABLE 1: ROE ANALYSIS

Benchmark	Expert	Description
	11.25	Hevert – high end of range
11.15		**Highest Awarded ROE (last 12 months, national)**
	10.70	Hevert Recommendation
	10.40	Hevert – low end of range
10.30		**Average (last 12 months, national)**
10.20		**Average (last 12 months, states bordering Missouri)**
10.18		**Average (calculated at hearing – 7 un-restructured utilities)**
10.00		*ROE awarded to KCPL/GMO*
	9.90	Gorman, LaConte Recommendation
9.30		**Lowest Awarded ROE (last 12 months, national)**
	9.25	Murray – high end of range
	8.75	Murray Recommendation

U.S. 467, 499 n. 17, 122 S.Ct. 1646, 1666 n. 17, 152 L.Ed.2d 701, ___ (2002) ("Opportunity cost" . . . is "the value of the best forgone alternative use of the resources employed"), *quoting* D. Carlton & J. Perloff, ***Modern Industrial Organization*** (2nd ed. 1994), p. 56.

[86] *Staff's Initial Brief,* p. 58 n. 132.

[87] The allowed ROE is a different quantity than either the market-required return or the Lowest Reasonable Rate. The allowed ROE is the final product of the Commission's work and it is the result of the second analytical step; the Lowest Reasonable Rate, by contrast, is the result of the first analytical step in the two-step process described by the Supreme Court.

(however defined), preferably at 10.7%; for MIEC and MEG, the desired allowed ROE is somewhat below the average at 9.9%. The truth of Staff's assertion is apparent from the fact that each expert recommended a *range,* only the low end of which can be considered to be the Lowest Reasonable Rate.

It is useful to consider the experts' recommendations in the light of various benchmarks developed during the hearing on this case.[88] Table 1 shows that all of the experts except Mr. Murray have produced recommendations comfortably above the lowest ROE awarded to an electric utility in the nation over the past twelve months, 9.3% to Niagara Mohawk Power in January 2011.[89] Mr. Hevert's recommendation is well above all three of the average figures; in fact, the *bottom* of his recommended range exceeds all three of the averages.[90] It should be immediately apparent that so high a figure cannot possibly be the Lowest Reasonable Rate. Mr. Hevert's range reflects, instead, the allowed ROE that his client seeks. The high end of Mr. Murray's range, on the other hand, is almost identical to the lowest awarded ROE. The Commission can thus be confident that Mr. Murray has identified the Lowest Reasonable Rate.

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[88] Sources: Highest & Lowest Awards: Ex's 238 & 239; Hevert recommendation (revised): Ex. 123:68; Hevert lowest reasonable rate: AmMo Initial Brief, pp. 3, 11, Ex. 123:8, *and see* Tr. 22:1076 (admission by counsel for AmMo in his opening statement); National Average & Average for States Neighboring Missouri: AmMo Initial Brief, pp. 12-13; Average calculated at hearing: Tr. 22:1254; MoPSC ROE Awarded to KCPL/GMO: *Report & Order,* Case No. ER-2010-0355, issued April 12, 2011, at p. 124, *and see* Tr. 22:1075 (admission by counsel for AmMo in his opening statement); Gorman recommendation (revised): Ex. 409:18-19; LaConte recommendation (revised): Ex. 452:8.

[89] Ex. 238:4.

[90] Why three averages? 10.3% is the national average over the past twelve months; 10.2% is the average in states neighboring Missouri over the past twelve months and 10.18% is the average calculated by Mr. Gorman at the hearing in response to questions by Commissioner Davis, based on 1Q 2011 data from Ex. 238.

Mr. Murray's recommended ROE range is based on utility investors' required returns on equity, not on "expected" outcomes used by investors for cash modeling or "desired" outcomes preferred by particular parties. AmMo did its best to confuse the record on this issue, but Mr. Murray explained that financial experts and investors would not need a glossary of terms to understand the meaning of "required returns" on equity when reviewing equity research. It is not surprising that AmMo would attempt to confuse the issue as the required returns on equity for utility companies provided by Bank of America/Merrill Lynch's were no higher than 8.8%.[91] And this was not the only third-party information that corroborated Mr. Murray's single-digit cost-of-equity estimation.

As usual, Mr. Murray marshaled an impressive array of corroborating evidence in support of his recommendation, which AmMo has taken pains to explain away.[92] Mr. Murray has demonstrated that estimations of the cost of AmMo's equity capital that are undertaken for asset valuation purposes are strikingly lower than those offered by ROE experts in rate cases. AmMo seeks to avoid the inevitable conclusion to be drawn from this evidence by suggesting that the two estimation tasks are "fundamentally different." Indeed they are – one has to do with spending the client's money while the other allows the client to get the ratepayers' money. The only fundamental difference is *qui bono,* "who benefits." When it is to AmMo's benefit, the cost of equity is high – somewhere between

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[91] Ex. 241, p. 56.

[92] Ex. 219, pp. 8-13 (Duff & Phelps valuation); Ex. 220, pp. 2-9 (Lazard valuation); Ex. 241, p. 56 (Bank of America/Merrill-Lynch Report: required return for electric utility equity is 8.8%).

10.40% and 11.25%; when it is not, then the cost of equity **is even lower than the bottom of Mr. Murray's recommended range.** AmMo's attempt to persuade the Commission that the estimation of the cost of equity capital in the asset valuation context is somehow fundamentally different from the ratemaking context is nonsensical and should be ignored.[93] In fact, before Mr. Hevert realized the striking difference between the cost of equity estimates Ameren and its financial advisors used for internal valuation and financial reporting purposes, he freely admitted that the cost of equity in ratemaking and valuation are based on the same fundamentals.[94]

Is there any justification for an ROE above the Lowest Reasonable Rate?

Only appropriate regulatory purposes, based on substantial evidence of record, can justify an ROE higher than the Lowest Reasonable Rate. In other words, while the Commission has discretion to set the ROE anywhere in the zone of reasonableness that extends upwards from the Lowest Reasonable Rate, it is not an unfettered discretion. The short answer to the question posed above is "no," there is no justification in the record for an elevated allowed ROE for AmMo.

AmMo has argued several theories to justify an ROE above the Lowest Reasonable Rate:

- The Company has emphasized its historic inability to actually earn

[93] Mr. Gorman did not agree, for example. Tr. 22:1224-25.

[94] Ex. 219, p. 16, ll. 20-21, through p. 17, ll. 1-5.

its allowed ROE. Staff points out, emphatically, that circumstance is *not* the sort of permissible regulatory purpose that justifies a higher allowed ROE.

- AmMo argues that current market conditions require an ROE above the national average because (1) less equity capital is available than before the financial market crisis and recession and (2) investors are more risk averse than before the recession.
- AmMo suggests that it faces two unusual risks that justify a higher ROE: regulatory risk and coal-reliance risk. First, AmMo contends that the credit community attributes a higher regulatory risk to AmMo than to Mr. Hevert's proxy group and that this above-average regulatory risk supports an above-average authorized ROE.[95] Second, AmMo contends that an above-average ROE is appropriate because it obtains a materially-larger percentage of its generation from coal-fired plants (76.61%) than the proxy group average (63.57%).[96] AmMo contends, "[t]he rising costs associated with environmental compliance for utilities such as Ameren Missouri that are dependent on coal-fired generation – and the associated risks to the utility's financial performance – should be acknowledged."[97]

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[95] AmMo Initial Brief, p. 19.

[96] *Id.,* at p. 20.

[97] *Id.*

AmMo's Inability to Actually Earn its Authorized ROE:

AmMo's CEO, Warner Baxter, testified at length concerning the effects of regulatory lag, chief of which is AmMo's historic inability to actually earn its allowed ROE.[98] The causes, in addition to the current rising-cost environment, are structural: Missouri's 11-month rate case cycle; Missouri's traditional reliance on a historical test year; Missouri's insistence on building an incentive into the FAC;[99] Missouri's anti-CWIP statute.[100] Regulatory lag, as this Commission has frequently had occasion to observe, is no reason to raise rates: in a declining-cost environment, AmMo would be reaping the benefit of regulatory lag.

Current Market Conditions:

Staff expert David Murray provided a comprehensive review of current market conditions in Staff's *Revenue Requirement Cost-of-Service Report.*[101] Nothing in that report supports AmMo's claims. The economy is expanding, but at a slower rate than before the crisis of 2008 and the recession that followed it.[102] Interest rates are at historic low levels.[103] "Utility debt markets continue to indicate a fairly low cost-of-capital environment."[104] Long-term utility bond yields

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[98] "Regulatory lag" is the interval between a change in revenue requirement and its reflection in rates. *See* Ex. 100, Baxter Direct, pp. 16-22.

[99] "FAC" is Fuel Adjustment Clause, a mechanism intended to reduce the utility's vulnerability to fuel-cost volatility.

[100] "CWIP" is Construction Work in Progress; the anti-CWIP statute at XXX prohibits the inclusion of any costs for electric utility plant that is not yet "used-and-useful" in rates.

[101] Ex. 201, pp. 7-10.

[102] *Id.,* at p. 7.

[103] *Id.*

[104] *Id.,* at p. 8.

have increased somewhat after reaching a 40-year low in August and September of 2010.[105] The cost of investment-grade utility debt capital has reached historic lows and utilities with investment-grade credit ratings – like AmMo -- can obtain capital quite cheaply.[106] In the utility equity market, the higher return on "Regulated" electric utilities compared to broader markets and "Diversified" electric utilities reveals that, because of the "flight to quality," the cost of equity for utilities like AmMo has decreased.[107] The decrease in bond yields confirms this picture.[108] The upshot is, AmMo is trying to sell the Commission a bill of goods. Equity investors are indeed more risk averse, so they are flocking to safe harbors such as integrated, regulated, electric utilities such as AmMo. These facts do not support an allowed ROE greater than the Lowest Reasonable Rate.

These facts also belie AmMo's contention that it will be unable to attract capital if its ROE is set lower than 10.40%. As the preceding discussion shows, utility equity is hot right now. In fact a recent *Wall Street Journal* article went as far as to imply that utility stocks were "sexy."[109] Investors want it because it's safe. As the economic recovery continues to sputter, that will not change. AmMo simply does not need an elevated ROE to attract equity capital.

Elevated Regulatory Risk:

Mr. Murray also provided a comprehensive survey of AmMo's credit rating

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[105] *Id.*

[106] *Id.,* at p. 9.

[107] *Id.,* at pp. 9-10.

[108] *Id.*

[109] Ex. 201, p. 10, ll. 11-16.

in Staff's *Revenue Requirement Cost-of-Service Report.*[110] In December 2010, Standard & Poor's ("S&P") referred to AmMo's "excellent business risk profile [that] reflects its recent rate cases and regulatory mechanisms that overall **indicate a decreasing regulatory risk.**[111] The Commission was described by S&P as having given AmMo "credit supportive rate case orders."[112] AmMo's claim that elevated regulatory risk supports a higher allowed ROE for AmMo is revealed as nonsense.

Elevated Coal-Reliance Risk:

AmMo's own discussion of its elevated coal-reliance risk is filled with suppositions and maybes. Yes, AmMo's high reliance on coal may cost it money **in the future.** But that is not the case today, as is amply evidenced by AmMo's complete failure to identify any present impacts of high coal-reliance. If anything, the Commission should focus on the reduced risk AmMo enjoys under the regulatory compact that permits it to recover increased costs through increased rates. If AmMo's operating costs rise due to its reliance on coal-based generation, **AmMo's rates will necessarily rise as well.** The record on this point does not support an elevated allowed ROE.

Conclusion:

To meet constitutional requirements, the Commission must first identify

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[110] Ex. 201, pp. 12-14.

[111] *Id.,* at p. 13 (*quoting* S&P credit report on Ameren Missouri, December 28, 2010). (Emphasis added.)

[112] *Id.*

the Lowest Reasonable Rate and then determine whether the record supports an allowed ROE higher than the Lowest Reasonable Rate. The Lowest Reasonable Rate is somewhere in the range proposed by Mr. Murray, 8.25% to 9.25%, as is conclusively established by Ameren's internal cost-of-equity estimates and the testimony of Mr. Gorman and Ms. LaConte showing that equity investors simply do not require an ROE anywhere above 10.00%. Although AmMo desperately desires a higher allowed ROE, it has utterly failed to show any evidence supporting a higher allowed ROE. Although it has argued that current market conditions, capital attraction, regulatory risk, and coal-reliance risk all support an "above-average authorized ROE," the fact is that AmMo has failed to show that it qualifies for even an average ROE. Although AmMo's Initial Brief implies that the sky will fall if it is authorized an ROE below 10.40%, to Staff's knowledge the sky has not fallen on the west side of the state, where the Commission just last month authorized an ROE of 10.00% for Kansas City Power & Light Company and KCP&L Greater Missouri Operations Company. Mr. Murray's single-digit cost of equity estimates are supported not only by his analysis, but are corroborated by Ameren's own internal valuation analysis and the analysis of equity analysts that presumably influence the investment decisions of investors.

Just as Mr. Murray, together with Ms. LaConte and Mr. Gorman testified, AmMo's allowed ROE must in no case be higher than 10.00%. In fact, it should be quite a bit lower – below 9.25%.

8. Fuel Adjustment Clause Issues:

A. Should the Commission authorize Ameren Missouri to continue its current Fuel Adjustment Clause (FAC) or should the Commission discontinue or order modifications to the FAC?[113]

B. Should the sharing percentage in Ameren Missouri's FAC be changed from 95/5 percent to 85/15 percent?

C. Should the length of the recovery periods for the FAC be reduced from twelve (12) months to eight (8) months?

D. Should the Company have the ability to adjust the FPAC rate for errors in calculations that may have occurred since the FAC Rider was granted to Ameren Missouri?

E. What is the appropriate tariff language to reflect any modifications or clarifications to Ameren Missouri's FAC?

Correction to initial brief:

On page 77 of its initial brief Staff stated, "The use of data at the transmission level versus the generation level resulted in Ameren Missouri's NBFC rates being lower than if the net system input would have been used." That sentence, instead, should read, "The use of data at the transmission level versus the generation level resulted in Ameren Missouri's NBFC rates being higher than if the net system input would have been used." Staff regrets any confusion this error may have caused.

Correction to testimony:

On page 86 of its initial brief Ameren Missouri essentially quotes from the surrebuttal testimony of Staff witness Roos when it states the following, "He also

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[113] The Company does not believe that this issue has properly been raised in this case, nor that it is an issue that requires resolution by the Commission in this case. Other parties disagree.

argued that since Staff has only 30 days to review the true-up filing, the addition of this language could result in a delay in returning/billing the difference between what was to be collected and what was actually billed in the accumulation period." The reference to "accumulation period" in the foregoing sentence should be "recovery period," since neither credits nor billings are made during accumulation periods in Ameren Missouri's FAC. The error originates from line six on page four of his surrebuttal testimony (Ex. 225) and was not corrected during the hearing. Staff regrets not having caught and corrected this error earlier, but believes it has no impact on the arguments briefed.

Introduction:

The parties to which Staff is replying in this brief regarding FAC issues are AARP, Consumer's Council of Missouri, the Missouri Industrial Energy Consumers and Ameren Missouri. AARP and Consumer's Council of Missouri both argue for discontinuance of Ameren Missouri's FAC. MIEC argue against shortening the recovery periods from twelve to eight months. Ameren Missouri argues against changing the sharing from 95%/5% to 85%/15% and for the addition of language in its tariff to allow the correction of "errors" during the true-up phase. Staff responds to each in the order in which the issues are presented at the beginning of this section of its brief above. Much like return on equity, on these issues reasonable persons could reach very different determinations, and this Commission is vested with wide discretion in deciding them.

Continuation, Discontinuation or Modification of the FAC:

Both AARP and Consumer's Council of Missouri argue Ameren Missouri has the burden of showing its FAC should be continued and that Ameren Missouri's FAC should be discontinued. They argue it should be discontinued because, although permitted by law, "it is a single-issue surcharge that is unfair to consumers and because of the severe damage such mechanisms do to the utility's incentive to be efficient" and it is "ill-suited to [Ameren Missouri's] operations which benefit from ample off-system sales opportunities to help it hedge against fuel cost volatility."[114]

Even though Ameren Missouri structured its contracts with AEP and Wabash in an effort to circumvent its FAC, because of the tens of millions of dollars its actual fuel and purchased power costs have varied from those embedded in its general rates, as shown on the tables on page 109 of the Staff's Revenue Requirement Cost of Service Report (Ex. 201) and Schedule LMM-S1-1 to the surrebuttal testimony of Staff witness Lena M. Mantle (Ex. 218), Staff is not recommending the Commission discontinue Ameren Missouri's FAC. However, Staff is recommending Ameren Missouri's FAC be modified to have an 85%/15% sharing rather than a 95%/5% sharing.

Sharing Mechanism:

On pages 77 to 84 of its initial brief, Ameren Missouri argues that it is sufficiently incented to take all reasonable actions to keep fuel and purchased

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[114] AARP Initial Brief, p. 8, Consumer's Council of Missouri Initial Brief, p. 8.

power costs as low as possible by the combination of the 95%/5% sharing, the mandated regular prudency reviews and the Commission's authority to discontinue its FAC. Staff disagrees.

With regard to changing the sharing from 95%/5% to 85%/15%, Ameren Missouri asserts that no one has alleged or found it has been imprudent in managing its net fuel costs while it has had a FAC, and that it would be unfair for Ameren Missouri to "absorb" more than the five percent it presently does not recover when its costs increase above those embedded in general rates and the NBFC rates in its FAC.

Ameren Missouri's argument is premised on the starting point for designing its FAC is that the Commission should allow Ameren Missouri to recover all of its fuel and purchased power costs that differ from the amount predicted by its NBFC rates. Staff believes the more appropriate perspective is that the Commission is allowing Ameren Missouri to recover the portion of its fuel and purchased power costs that differ from the amount predicted by its NBFC rates while giving Ameren Missouri a sufficient incentive to improve the efficiency and cost-effectiveness of its fuel and purchased power costs, *i.e.*, to ***minimize*** its fuel and purchased power costs. Staff's view is supported by section 386.266.1, RSMo. Supp. 2010, which provides:

> Subject to the requirements of this section, any electrical corporation may make an application to the commission to approve rate schedules authorizing an interim energy charge, or periodic rate adjustments outside of general rate proceedings to reflect increases and decreases in its prudently incurred fuel and purchased-power costs, including transportation. The commission may, in accordance with existing law, include in such rate

> schedules features designed to provide the electrical corporation with incentives to improve the efficiency and cost-effectiveness of its fuel and purchased-power procurement activities.

As Staff briefed in the recent general rate increase case of KCP&L Greater Missouri Operations Company (Case No. ER-2010-0356), the link the Legislature has forged between incentives and fuel and purchased-power procurement is that the Commission may include features designed to provide the electrical corporation with incentives to improve the efficiency and cost-effectiveness of its fuel and purchased-power procurement activities. The Legislature did not link a finding of no imprudence to a "sharing" mechanism.

Staff's goal in recommending an 85%/15% sharing is not to deprive Ameren Missouri of revenue, as it implies by its references to "absorbing prudently incurred costs," but to give Ameren Missouri enough financial incentive for it to minimize the amounts of the credits and charges made to its customers through its FAC.

When the Commission first adopted the 95%/5% sharing for Ameren Missouri's FAC to provide Ameren Missouri with an incentive to improve the efficiency and cost-effectiveness of its fuel and purchased power procurement activities, it was the beginning of an "experiment" that has been very expensive to Ameren Missouri's ratepayers. In the following Ameren Missouri rate case, its immediately prior rate case, the Commission requested the parties to address not only whether the 95%/5% sharing provided Ameren Missouri with sufficient financial incentive to be prudent in its fuel and purchased power costs, but also whether it provided Ameren Missouri sufficient incentive to take reasonable

efforts to minimize its fuel and purchased power costs. Staff's Revenue Requirement Cost of Service Report, p. 107 (Ex. 201).

Now that the 95%/5% sharing has been in Ameren Missouri's FAC for six accumulation periods, there is sufficient history for Staff to conclude that a 95%/5% level of sharing does not provide Ameren Missouri with sufficient financial incentive to minimize the amounts of the credits and charges from its FAC, *i.e.*, the 95%/5% level of sharing does not provide Ameren Missouri with sufficient financial incentive to determine the most appropriate NBFC rates and to minimize its fuel and purchased power costs. That is why Staff is recommending Ameren Missouri's sharing be changed to 85%/15%.

Ameren Missouri's calculation of the impact of changing its sharing from 95%/5% to 85%/15% for historical accumulation periods is based on assumptions both that changing the sharing would not change the precision of the NBFC rates and that Ameren Missouri could not have minimized its fuel and purchased power costs below the costs it actually incurred. Given those assumptions, and that Ameren Missouri fuel and purchased power costs increased during five of its six historical accumulation periods, Ameren Missouri necessarily would have recaptured fewer of its actual fuel and purchased power costs with an 85%/15% sharing. Therefore, Ameren Missouri's argument distills down to simply that because no one has asserted or shown imprudence in its fuel and purchased power transactions, the FAC sharing should not be changed from the current 95%/5%. Staff disagrees that this is the only factor the Commission should consider when determining the sharing.

Staff is recommending the sharing be changed from 95%/5% to 85%/15% because, despite what Ameren Missouri characterizes as "powerful incentives"—the regular prudence reviews, the Commission's authority to discontinue its FAC, and the 95%/5% sharing currently in its FAC—Ameren Missouri was not dissuaded from relying on fuel run energy for setting NBFC rates in Case No. ER-2008-0318, which resulted in those rates being too high. In addition, Ameren Missouri's coal purchases are no longer pooled with Ameren Genco's coal purchases. That was one of the factors the Commission relied on in Ameren Missouri's last rate case to determine Ameren Missouri had sufficient incentive to minimize its coal costs. Perhaps most significantly for this case, in their rebuttal testimony prefiled on March 25, 2011, and admitted into evidence in this case on May 4[115] and April 27,[116] 2011, respectively, Ameren Missouri witnesses Jaime Haro and Lynn Barnes testified that Ameren Missouri believes the three-year average of power prices used to derive off-system sales revenues results in those revenues is overstated. This means Ameren Missouri believes the off-system sales revenues it agreed to in the *Third Non-Unanimous Stipulation and Agreement* filed May 6, 2011, which the Commission approved with its *Order Approving Stipulations and Agreements* on June 1, 2011, are overstated resulting in a net fuel and purchase power expense that is higher than what Ameren believes is correct. It also means Ameren Missouri believes the NBFC rates it also agreed to in that stipulation and agreement are understated by those

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[115] Tr. Vol. 24, p. 1477 (Haro).

[116] Tr. Vol. 18, pp. 331-34 (Barnes).

same off-system sales revenues.[117] In other words, the 95%/5% sharing has not sufficiently incented Ameren Missouri to determine appropriate NBFC rates in this case and to improve the efficiency and cost-effectiveness of its fuel and purchased power procurement activities. If its NBFC rates are too low, as Ameren Missouri believes, then, assuming its fuel and purchased power costs are not decreasing, its current 95%/5% sharing will allow Ameren Missouri to recover only 95% of the difference resulting from the NBFC rates being too low, *i.e.,* instead of collecting 100% of the fuel cost in the permanent rates, Ameren Missouri will only recover what was included in the permanent rates plus 95% of the difference between the net fuel and purchased power cost it agreed to and what it believes is accurate. If the sharing was 85%/15% it would increase Ameren Missouri's incentive to minimize any error in setting the NBFC rates in such an environment since it would then forego 15% of the difference rather than 5%.

While, like KCP&L Greater Missouri Operations Company, Ameren Missouri dwells on the potential impact to its revenues based on its past experience—where Staff believes it was inadequately incented—it ignores the potential benefits from the 15% of off-system sales revenues it would get under Staff's proposal, a benefit Staff believes better incents Ameren Missouri to "improve the efficiency and cost-effectiveness of its fuel and purchased-power procurement activities." Changing Ameren Missouri's sharing in its FAC to

[117] Ex. 103, Barnes Rebuttal, p. 8, ll. 1-13; Ex. 125, Haro Rebuttal, pp. 3-5.

85%/15% will give Ameren Missouri a strong incentive to both accurately determine NBFC rates and reduce its future fuel and purchased power costs.

As Staff has previously stated, the purpose of a fuel adjustment clause is to protect a utility from the regulatory lag associated with recovery through retail rates of increasing fuel-related costs and its customers from the regulatory lag associated with reductions in retail rates due to decreasing fuel-related costs. With a sharing mechanism, even if there is no mismatch between the utility's actual fuel costs and purchased power costs and the fuel and purchased power costs used to establish the base rates in its fuel adjustment clause—for Ameren Missouri NBFC rates—if they do not accurately match its actual costs, then the sharing mechanism will from the start cause the utility to either over- or under-recover the changes in its fuel and purchased power costs. If Ameren Missouri is correct and its actual fuel-related costs are higher than what it agreed to, Ameren Missouri will only recover its sharing percentage of the difference between the fuel and purchased power costs that should have been used for setting its NBFC rates and the costs Ameren Missouri, and the other parties, agreed to.

When the Commission looks beyond the single factor that no one has alleged or found Ameren Missouri has imprudently managed its net fuel costs while it has had a FAC and considers the other factors Staff has raised above and in its initial brief, Staff is confident the Commission will adopt Staff's recommendation that it modify the sharing in Ameren Missouri's FAC from 95%/5% to 85%/15%.

Length of FAC Recovery Periods

At pages 24-25 of their initial brief, the Missouri Industrial Energy Consumers argue against shortening the recovery periods of Ameren Missouri's FAC from twelve to eight months. As Staff understands their argument, MIEC are arguing a twelve-month recovery period moderates the impacts of the recovery or credit on customers who may have seasonal variations in usage. Staff does not disagree that by shortening the recovery period, when it has under-collected its fuel and purchased power costs in general rates, Ameren Missouri will collect more money sooner—eight months rather than twelve. However, when Ameren Missouri has over-collected its fuel and purchased power costs in general rates, it will also return more money to its customers sooner. Staff is comfortable that it can process the FPA changes sufficiently quickly to move to an eight-month recovery period; it would not have proposed the modification otherwise. Shortening the recovery periods will reduce regulatory lag, reduce the short-term borrowing rate interest customers pay on charges or receive through credits and will send price signals to customers better correlated with the fuel and purchased power costs Ameren Missouri incurs to serve them. For all these reasons Staff recommends the Commission modify the recovery periods of Ameren Missouri's FAC to be eight months rather than twelve.

Tariff Provision to Authorize "Error Correction" in True-Up

Undoubtedly because Staff is opposing, in File No. ER-2010-0274, Ameren Missouri's request to be allowed to bill additional revenues as an

adjustment to its true-up filing due to the NBFC rates the Commission ordered in File No. ER-2008-0318 not being properly calculated—at least Staff does not believe Ameren Missouri is suggesting the monies it over-collected due to its imprudence the Commission determined in File No. EO-2010-0255 be corrected in a true-up—Ameren Missouri is seeking a provision in its tariff that would allow in the true-up proceedings consideration of matters beyond the difference between what was intended to be billed (charged or credited) to customers during a recovery period and what was billed (charged or credited) to customers during that recovery period. In practice, Ameren Missouri is asking the Commission to create uncertainty in its FAC through an open-ended ability to modify the interpretation and potentially the content of Commission-approved FAC tariff sheets whenever the Commission determines an error has been made. Staff stridently disagrees with Ameren Missouri that its fuel adjustment clause is, or should be, perpetually open to revisions.

As it has consistently argued in cases such as File No. ER-2010-0274 and File No. ER-2010-0255, it is Staff's position that certain aspects of fuel adjustment clauses are fixed in general rate cases and remain unchanged until changed in a subsequent general rate case—for example the NBFC rates in Ameren Missouri's FAC. Staff has also consistently argued that the only consideration in a true-up proceeding is to determine the over- or under-billing (charge or credit) that occurred in a recovery period, *i.e.*, what is the difference between was intended to be billed (charged or credited) and what was billed (charged or credited) during the recovery period. Staff has also consistently

argued that a prudence review is the last review of the operation of a fuel adjustment clause for the period reviewed. For example, had Staff not raised the issue of Ameren Missouri's compliance with the FAC provisions of its tariff in its prudence review in File No. ER-2010-0255, it is Staff's view the matter could not have been raised later, *i.e.,* there is finality for the period covered in a prudence review. Apparently Ameren Missouri also finds some measure of finality in prudence reviews, since it so stridently argues them as its basis for not changing its sharing mechanism.

Ameren Missouri's position is that there is never any finality for any time period for its fuel adjustment clause. Staff simply disagrees. Further, as Staff witness Roos testified, because only 30 days are allowed for Staff's review of a true-up filing, the true-up process is intended and designed only to review the difference between what was intended to be billed (charged or credited) and what was billed (charged or credited) during a recovery period. During true-up reviews, Staff does not have the resources to be continually meeting with utilities such as Ameren Missouri or have time for multiple rounds of data requests to reach understandings of what the utility asserts is erroneous.[118] The time for finding errors is before charges or credits are implemented for the recovery period associated with an accumulation period, not in a subsequent true-up, prudence or other review. The Commission should give Ameren Missouri ample incentive to do so. Further, as Staff argued in File No. ER-2010-0274, any

[118] Ex. 225, Roos Surrebuttal, pp. 4-5.

claimed error in a final Commission order, *e.g.* ordered NBFC rates, simply cannot be "corrected" in a true-up, or any other FAC proceeding. However, errors that involve prudence are subject to being reviewed during in a prudence review.

Staff recommends the Commission reject Ameren Missouri's proposal to expand the scope of its FAC true-up reviews.

9. LED Lighting:[119]

Energy efficiency is of growing concern, as evidenced not only by increasing customer participation levels in DSM programs[120], but also by Missouri's legislative direction[121]. Municipal customers within AmMo's service territory have expressed a desire to have other street and area lighting (SAL) system options available to them.[122] Yet, AmMo remains uncommitted to filing a LED lighting tariff.

Currently, AmMo has approximately 212,800 SAL systems for the 1,568 public street and municipal lighting customers in its service territory, using a total of about 137,000 MWh according to its 2009 Annual Report.[123] Most of the existing lighting in the Company's service area is old technology consisting of high pressure sodium (HPS) lamps or mercury vapor (MV) lamps,[124] while, the

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[119] "LED" means Light Emitting Diode.

[120] Direct Testimony of John A. Rogers, Ex. 201, p. 35, l. 18 - p. 43; Sch's JAR-1 and JAR-2.

[121] Missouri Energy Efficiency Investment Act, § 393.1075 RSMo (Supp. 2010).

[122] Surrebuttal Testimony of Dr. Hojong Kang, Ex. 215, p. 2, ll. 7-13; Sch. HK-1.

[123] Staff Rate Design and Class COS Report, Ex. 204, p. 33, ll. 4-7.

[124] *Id.,* at ll. 16-19.

LED lighting fixtures proposed for use by the Staff in the Company's SALs are the most energy efficient fixtures available today[125]. Even the Company has admitted to the energy savings possible by using LED fixtures in its current Chapter 22 Electric Utility Resource Plan compliance filing, File No. EO-2011-0271. The Company stated in its resource plan filing:

> Thus far, the project has yielded measurable energy savings and noticeable light quality differences (as seen above). The energy savings associated with the project are in the graph below. The values represent 3 lights on a single circuit indicating the baseline units are using roughly 300 watts per unit (with ballast). *The efficient replacement is using approximately 185 watts per unit, equating to a 40% energy savings on the three metered lights.*[126]

AmMo also presented at the Rural Electricity Resource Council's November 2010 conference that it valued LED lighting because it wanted to "[b]ecome a national best practice leader in outdoor LED lighting" and to "[s]how to our customers we are their **Trusted Energy Advisor**."[127] The Staff's recommendation seeks for AmMo to commit to a date to file a tariff for the use of LED SALs in its service territory.

AmMo stated in its brief that "…because a stipulation and agreement approved in Case No. ER-2010-0355 obligates the Commission to sponsor a workshop on a broad range of outdoor lighting issues, including LED lighting, the Company believes that it would be premature, imprudent, and unfair to require

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[125] *Id.,* at p. 34, ll. 1-11.

[126] Ex. 215, Surrebuttal Testimony of Hojong Kang, p. 2 , ll. 14-19 (emphasis added); Sch. HK-2.

[127] *Id.*; Sch. HK-3-2. (emphasis in original).

Ameren Missouri to take any action on that issue prior to the completion of the workshop."[128] AmMo witnesses also cited at hearing the Commission's order adopting the stipulation and agreement. The stipulation and agreement entered into by the parties does not "obligate" the Commission to open a docket regarding the Outdoor Lighting issue, it only "recommends" that the Commission do so.[129] It is a bold statement for AmMo to suggest that just because a party recommends the Commission do something that it must then do the requested act. Even if the Commission were to host a workshop, there is no guarantee that the workshop will produce a commitment on AmMo's part to file a tariff, regardless of how productive the workshop may prove to be. It would be "unfair," using AmMo's word, not to require the Company to commit to a tariff filing as the other Missouri electric companies have committed to do.

AmMo failed to mention for the Commission's information and consideration that both Kansas City Power & Light Company (KCP&L) and KCP&L – Greater Missouri Operations Company (GMO) stipulated to file a LED lighting tariff by the end of 2012, or indicate when they intend to complete such filing:

> Both KCPL and GMO agree they shall file by the end of calendar year 2012 either a LED lighting tariff, or when the Companies anticipate filing such LED lighting tariff. Also, by the end of calendar year 2012, both KCPL and GMO shall file the results of its LED

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[128] Initial Post-Hearing Brief of Ameren Missouri, p. 125.

[129] ER-2010-0355, Non-Unanimous Stipulation and Agreement As To Outdoor Lighting Issues, p. 2; ER-2010-0355, Report and Order, p. 9.

> study, which shall include a review of potential LED lighting health issues.[130]

Also, The Empire District Electric Company (Empire) entered into a *Global Agreement* that the Commission adopted by Order in Case No. ER-2011-0004. Paragraph ten (10) of that public *Global Agreement* states that "[w]ithin one year of effective dates of rates in this case, Empire agrees to file either LED lighting tariff sheets or an update on a LED pilot study and plans for filing future tariff sheets." At this point in time, AmMo is the ***only*** electric company regulated by this Commission that has not committed to filing a LED lighting tariff or telling the Commission why it is impractical.

The Staff is not rushing AmMo to a decision on LED lighting as the Company claims.[131] The Staff's recommendation allows the Company to report to the Staff at the end of the twelve (12) month period should the Company need more time to file. Nor is the Staff attempting to commit AmMo to a LED program where it cannot recover any prudent and reasonable costs incurred. The Staff anticipates the Company filing a tariff for the Staff's review that allows the recovery of the prudent and reasonable costs associated with LED lighting and a return on the Company's investment. AmMo's initial data and comments on LED lighting show cost-effective results.[132] It is illogical for the Company to suggest

[130] ER-2010-0355, Tr. Vol. 34, p. 3715, l. 24 – p. 3716, l. 11.

[131] Initial Post-Hearing Brief of Ameren Missouri, p. 127.

[132] Ex. 215, Surrebuttal Testimony of Hojong Kang, p. 2, 11. 14-19; Sch. HK-2.

the use of short-term alternatives when there is viable LED technology available for implementation.[133]

Therefore, the Staff recommends that the Commission order the same treatment for AmMo as KCPL, GMO and Empire have agreed to do; for AmMo to complete its evaluation of LED SAL systems, and no later than twelve (12) months following the Commission's Report and Order in this case file either a proposed LED lighting tariff(s) or an update to the Commission on when it will file a proposed LED lighting tariff(s).

10. Solar Rebates Accounting Authority Order (AAO):

A. What is the appropriate method -- RESRAM or an Accounting Authority Order (AAO) -- for Ameren Missouri to recover the costs it incurs for compliance with the Missouri Renewable Energy Standard (RES) after the true-up date in this case (February 28, 2011)?

B. If the Commission determines that an AAO is appropriate, should the Company be authorized in this case to implement an AAO to recover the costs it incurred for compliance with the RES before the true-up date in this case?

C. What amount of solar rebate costs should Ameren Missouri be allowed to include in the revenue requirement used to set rates in this case?

For brevity, the Staff will point the Commission back to its initial brief for a full discussion of its recommendation in this matter. However, the Staff wishes to reemphasize its use of the twelve (12) month calendar year, or planning year, data to calculate the amount of solar rebates to include in the Company's annual

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[133] Initial Post-Hearing Brief of Ameren Missouri, p. 127.

revenue requirement, as well as its recommendation that the Company recover solar rebate compliance costs through the use of the RESRAM.

Rule 4 CSR 240-20.100 (5)(A) states, "[t]he retail rate impact shall be calculated on an incremental basis for each *planning year* that includes the addition of renewable generation directly attributable to RES compliance through procurement or development of renewable energy resources, averaged over the succeeding ten (10) year period…." (emphasis added). AmMo argues in its brief that "Staff provided no justification for using the calendar year 2010 expenditure level except for stating that it is less than the 1% limitation."[134] This simply is not true. In compliance with the statute, the Staff used the Company's first full calendar year, or planning year, worth of data to calculate the level of expenses to include in this rate case.[135] The calendar year 2010 is the first full year during which the rebates were available. This results in an expense level of $487,782, reflecting a twelve-month period.[136]

AmMo further asserts that its recommendation to include the amount of solar rebates paid by the Company through the true-up is not unusual and the Staff "often uses the true-up level for many expenditures, leaving the recommendation to use the calendar year expenditure without support in the record."[137] While it is true that the Staff does true-up many expenses, in this

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[134] Initial Post-Hearing Brief of Ameren Missouri, p. 115.

[135] Rebuttal Testimony of Michael E. Taylor, Exh. 229, p.3, ll. 10-18.

[136] True Up Direct Testimony of Gary S. Weiss, Sch. GSW-TE18-110; Exh. 202, Staff's Accounting Schedule 10, p. 17.

[137] Initial Post-Hearing Brief of Ameren Missouri, p. 115.

instance, there is a specific statute and rule to abide by that requires the use of the "planning year." Also, it is not the Staff's practice to include fourteen months of costs to calculate an annual expense level. The Staff has followed the rule and allowed $487,782 as expense in this case. The Staff recommends the remaining prudently-incurred compliance costs be carried forward and collected in future years as allowed in Section (6)(A).

Regarding the Company's request for an AAO to track compliance expense, the Staff recommends that the Commission order AmMo to use the more specific method for recovery, the RESRAM, as contemplated by both the Renewable Energy Standard Statute and the Commission's rules for the recovery of RES compliance costs.[138] AmMo argues in its brief that "there is no reason to not allow Ameren Missouri the AAO it seeks…"[139] In actuality, this position causes harm to the ratepayers through the Company's opportunity to recover a greater amount of carrying costs using an AAO. Why would the Company choose not to recover its expense more rapidly through a RESRAM, unless there was an opportunity to recover a greater amount of carrying costs using an AAO?

While the Company can use a RESRAM to recover expense outside a rate case,[140] the Company must wait to recover its expense through an AAO in

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[138] Rebuttal Testimony of Michael E. Taylor, Ex. 229, p.3, ll. 1-9.

[139] Initial Post-Hearing Brief of Ameren Missouri, p. 116.

[140] 4 CSR 240-20.100 (6)(C).

its next rate case.[141] Use of an AAO allows the Company during the interim between rate cases to defer ***all costs*** and place them in a regulatory asset account to earn a monthly carrying charge on the balance equal to its short-term cost of borrowing ***until the Company's next general rate case***. If the Company used the RESRAM, the Company would carry forward ***any costs over the one percent*** allowed rate impact, which would have a carrying cost applied monthly equal to the electric utility's cost of short-term borrowing rate. **Put simply, AMMO's proposal is a way for the Company to recover and earn a return on all its compliance costs rather than follow the RESRAM terms anticipated by the Commission rule.**

Therefore, the Staff recommends that the Commission order AmMo to use the more specific method for recovery, the RESRAM, as contemplated by both the Renewable Energy Standard Statute and the Commission's rules for the recovery of RES compliance costs and allow $487,782 as expense in this case.

11. Union Issues:

A. Does the Commission have the authority to order Ameren Missouri to do the following:

(1) Institute or expand its training programs within specified time periods as a means of investing in its employee infrastructure?

(2) Hire specific additional personnel within specified time periods as a means of investing in its employee infrastructure

(3) Submit to a tracker for its energy delivery distribution system?

(4) Submit to a tracker to address the need and efforts to replace the

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[141] 4 CSR 240-20.100 (6)(D)

aging workforce?

(5) Expend a substantial portion of the rate increase from this proceeding on investing and re-investing in its regular employee base in general, including hiring, training and utilizing its internal workforce to maintain its normal and sustained workload?
(6) Use a portion of the rate increase from this proceeding to replace equipment, wires and cable which have out lived their anticipated life?

B. If the Commission does have the authority, should it order Ameren Missouri to take one or more of the steps listed above?

Staff has not taken a position on these issues.

12. Property Tax:

Should the Commission order Ameren Missouri to return to its customers any reductions that the Company receives in its 2010 property taxes?

The Staff recommends that the Commission order AmMo to track its property tax expense and credit back to customers in the next rate case any reduction the Company receives in its 2010 paid property taxes. The Staff's revenue requirement included the amount of property tax expense paid by the Company based on its 2010 distributable property tax assessment. The Company is currently appealing the assessment before the Missouri State Tax Commission. The rates customers will pay based on this revenue requirement are designed to recover the 2010 property tax expense paid by the Company. Should AmMo receive a credit or refund for its level of 2010 property tax expense, it is only fair that the customers should also receive the corresponding amount as a credit in the next rate case.

AmMo has agreed to keep track of any refunds received from the appeal

and inform the parties in the next rate case of the amount.[142] While AmMo anticipates prevailing on its appeal[143], the Company argues the Commission should not order an automatic return of the full amount to its customers.[144] Instead, AmMo wishes to defer decision on this issue to the next rate case and "[a]t that time the amount of property tax refund, if any, will be known and the Company and all other parties to the future rate case can fully present all relevant evidence and arguments to the Commission for its consideration *and the issue of whether, and under what circumstances, the tax refund should be returned to customers*."[145] While at the same time collecting the 2010 tax amounts paid through the rates established in this case, the Company wants to preserve the right to argue in the next rate case that they should not credit back to customers the tax refund amount? This Commission should not allow AmMo to recover full 2010 property tax expense as a result of rates in this case without an assurance that the Company will return any over collected amounts back to the customers. As such, the Commission should order AmMo to track any tax amounts the State Tax Commission orders refunded back to the Company as part of the appeal case and provide a corresponding "credit" to the ratepayers in the next rate case.

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[142] Tr. Vol. 22, p.1331 ll. 9-17.

[143] Tr. Vol. 22, p. 1338, ll. 1-7.

[144] Initial Post-Hearing Brief of Ameren Missouri, p. 93.

[145] *Id.* (emphasis added).

13. Rate Design/Class Cost of Service

A. Class Cost of Service:

(1) Which of the proposed class cost of service methodologies – the 4 NCP–A&E methodology, the Base Intermediate-Peak methodology, or the 4P-P&A methodology – should the Commission use in this case to allocate Ameren Missouri's investment and costs among the Company's various rate classes?

(2) What methodology should the Commission use in this case to allocate Ameren Missouri's fixed production plant investment and operation and maintenance costs?

B. Rate Design:

(1) To what extent should the Commission rely on the results of a class cost of service study in apportioning revenue responsibility among Ameren Missouri's customer classes in this case?

(2) What amount of increase or decrease in the revenue responsibilities of Ameren Missouri's customer classes should the Commission order in this case?

(3) What is the appropriate monthly residential customer charge that should be set for Ameren Missouri in this case?

(4) Should Ameren Missouri be required to eliminate declining block rates for the residential winter energy charge? If so, should the declining block rates be eliminated in a revenue neutral manner?

Staff has no reply on these issues.

CONCLUSION

In conclusion, Staff recommends that the Commission grant Ameren Missouri a general rate increase amounting to approximately $92.8 million, resolving each contested issue as Staff has recommended. In this way, just and

reasonable rates will be set and all relevant factors considered, with due regard to the interests of the various parties and the public interest.

WHEREFORE, on account of all the foregoing, Staff prays that the Commission will issue its findings of fact and conclusions of law, determining just and reasonable rates and charges for Ameren Missouri as recommended by Staff herein; and granting such other and further relief as are just in the circumstances.

Respectfully submitted,

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Certificate of Service

I hereby certify that a true and correct copy of the foregoing was served, either electronically or by hand delivery or by First Class United States Mail, postage prepaid, on this **13th day of June, 2011,** on the parties of record as set out on the official Service List maintained by the Data Center of the Missouri Public Service Commission for this case.

s/ Kevin A. Thompson