

Exhibit No.:
Issues: Legal Fees,
Environmental Expense,
Injuries and Damages
Expense
Witness: John P. Cassidy
Sponsoring Party: MoPSC Staff
Type of Exhibit: Direct Testimony
Case No.: EC-2000- 795

MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

DIRECT TESTIMONY

OF

JOHN P. CASSIDY

FILED
MAY 30 2000
Missouri Public
Service Commission

UNION ELECTRIC COMPANY

CASE NO. EC-2000- 795

Jefferson City, Missouri
May, 2000

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JOHN P. CASSIDY
UNION ELECTRIC COMPANY
CASE NO. EC-2000-795

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1 A. Yes, I have. Please refer to Schedule 1, which is attached to my direct
2 testimony, for a list of cases in which I have previously filed testimony.

3 Q. With reference to Case No. EM-96-149, have you made an examination
4 of the data supporting the calculation of credits for the first sharing period of the second
5 experimental alternative regulation plan (EARP) and other books and records of Union
6 Electric Company (UE or Company)?

7 A. Yes, in conjunction with other members of the Commission Staff (Staff).

8 Q. What are your areas of responsibility in this case?

9 A. My areas of responsibility include the Staff's adjustments to UE's credit
10 calculation, for legal fees, environmental expense and injuries and damages expense.

11 Q. What adjustments are you sponsoring?

12 A. I am sponsoring the following adjustments, which appear on the
13 Adjustments to Income Statement, Accounting Schedule 10:

14	Legal Fees	S-9.3
15	Environmental Expense	S-9.4
16	Injuries and Damages Expense	S-9.6

17 **LEGAL FEES**

18 Q. Please explain how the Company accounts for the legal fees that the Staff
19 is adjusting.

20 A. The Company's treatment for these legal fees is based on accrual
21 accounting. Under this accrual basis, the Company maintains a reserve of accumulated
22 funds to pay for legal fees based on estimates of legal fees that the Company anticipates

1 will be incurred rather than for what is actually paid. Accruals to increase the reserve are
2 expensed and actual claims are charged against the reserve balance when paid.

3 Q. Please explain the Staff's proposed adjustment S-9.3 to legal fees.

4 A. During the first sharing period, July 1, 1998 through June 30, 1999, of the
5 second EARP, the Company accrued, for Missouri electric operations, approximately
6 \$2,677,190 of legal fees; however, the Company actually paid \$2,114,490 for legal fees
7 during the same period. This resulted in an excess accrual of \$562,699 for the
8 Company's Missouri electric operations, relating to legal fees. The Staff proposes to
9 remove the \$562,699 of excess accrual over actual cash payments, in order to treat legal
10 fees under a cash approach. The Staff's calculation of this adjustment is shown on
11 Schedule 2-1, which is attached to this direct testimony.

12 Q. Why does the Staff recommend a cash approach for the Company's legal
13 fees?

14 A. The Staff recommends a cash approach for the Company's legal fees in
15 order to avoid the excess accrual which has resulted during the current sharing period and
16 which could continue to exist during future periods of the EARP. The Staff's analysis
17 shows the excess accrual continued to increase through December of 1999. Additionally,
18 the cash approach will provide a determination of credits based on actual known costs
19 during the sharing period as opposed to the Company's accrual basis, which relies upon
20 an estimate of what actual future payments and costs will be. The Staff's adjustment is
21 reasonable because it allows the Company recovery of its actual legal fees payments
22 during the first sharing period of the second EARP.

23 Q. What is the Staff's justification for proposing this adjustment?

1 A. In Case No. EM-96-149, the Stipulation and Agreement states in sections
2 7.f.vi, 7.f.vii and 7.f.viii:

3 7.f.vi If Staff, OPC or other signatories find evidence that
4 operating results have been manipulated to reduce amounts
5 to be shared with customers or to misrepresent actual
6 earnings or expenses, Staff, OPC or other signatories may
7 file a complaint with the Commission requesting that a full
8 investigation and hearing be conducted regarding said
9 complaint. UE shall have the right to respond to such
10 request and present facts and argument as to why an
11 investigation is unwarranted.
12

13 7.f.vii UE, Staff, OPC and other signatories reserve the right to
14 bring issues which cannot be resolved by them, and which
15 are related to the operation or implementation of the Plan,
16 to the Commission for resolution. Examples include
17 disagreements as to the mechanics of calculating the
18 monitoring report, alleged violations of the Stipulation and
19 Agreement, alleged manipulation of earnings results, or
20 requests for information not previously maintained by UE.
21 An allegation of manipulation could include significant
22 variations in the level of expenses associated with any
23 category of cost, where no reasonable explanation has been
24 provided. The Commission will determine in the first
25 instance whether a question of manipulation exists and
26 whether that question should be heard by it.
27

28 7.f.viii Staff, OPC and other signatories have the right to present to
29 the Commission concerns over any category of cost that
30 has been included in UE's monitoring results and has not
31 been included previously in any ratemaking proceeding.
32

33 I would also note that the Reconciliation Procedure, Attachment C,
34 Section 2.g states, in part, that:

35 UE/Staff/OPC reserve the right to petition the Commission for
36 resolution of disputed issues relating to the operation or
37 implementation of this Plan.
38

1 All of these subsections are applicable to the Company's accrued legal
2 fees. The Staff believes that the difference between accrued legal fees and actual legal
3 fees payments is excessive and also represents a significant variation in expense with no
4 reasonable explanation. The Staff also believes that accruing expense at a higher level
5 than the actual cash payments incurred represents a reduction in amounts to be shared
6 with customers by the Company and therefore reflects a manipulation of earnings results
7 as covered in the Stipulation and Agreement. Finally, the Staff is unaware of any prior
8 rate case proceeding, involving UE, where legal expense accruals were at issue.

9 **ENVIRONMENTAL EXPENSE**

10 Q. What potential liability does the Company have for future environmental
11 costs?

12 A. The Company stated in its response to Staff Data Request No. 95 that it
13 will potentially incur future costs to clean-up several contaminated sites. In addition, the
14 Company also stated that it might incur future costs as a result of investigations by the
15 Missouri Department of Natural Resources on its manufactured gas plant sites.

16 Q. Please explain how the Company accounts for environmental expense.

17 A. Using an accrual basis of accounting, the Company maintains a reserve of
18 accumulated funds, which are set aside to pay for environmental costs related to clean-up
19 of contaminated sites.

20 Q. Please explain the Staff's adjustment S-9.4 to environmental expense.

21 A. During the first sharing period of the second EARP, the Company accrued
22 approximately \$2,000,000 for environmental expenses. During the same period, the
23 Company did not pay for any environmental costs. In fact, by the end of the first sharing

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John P. Cassidy

1 period of the second EARP, the Company had a total accrued balance of \$5,887,065 but
2 had not yet actually paid any money for environmental clean-up costs. The Staff
3 proposes to remove the \$2,000,000 of environmental expenses accrued by the Company
4 during the first sharing period of the second EARP and to treat these expenses under a
5 cash basis approach.

6 Q. Why does the Staff recommend a cash approach for the Company's
7 environmental expenses?

8 A. The Staff believes that ratepayers should begin paying for these costs only
9 when the amount and the timing of the liability incurred by the Company is more certain.
10 The Staff's adjustment is appropriate because it removes the additional accrual of
11 \$2,000,000 for an expense for which the Company has never made actual payments at
12 any time, including from the beginning of the first EARP, at July 1, 1995, through the
13 end of the first sharing period of the second EARP. Additionally, the Staff contends that
14 if any environmental costs are actually incurred in the future, there currently exists
15 approximately \$3,887,065 (\$5,887,065 minus \$2,000,000) to pay for such costs. The
16 Staff believes that this \$3,887,065 reserve for environmental costs is sufficient at this
17 point in time and that the additional \$2,000,000 accrual made during the first sharing
18 period of the second EARP should be eliminated.

19 Q. What explanation has the Company provided for its environmental
20 accruals and why is this explanation unreasonable?

21 A. The Company has indicated that it needs to make accruals now for these
22 potential future environmental costs. The Staff believes this is unreasonable because the
23 actual timing and the amount of these expenditures are unknown. Another variable that

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1 must be considered is how much money other liable entities to the clean-up, as well as
2 their insurance companies, will pay in order to help fund any possible future
3 environmental costs. Considering, the fact that the Company has already accrued an
4 environmental costs reserve totaling \$3,887,065, despite not having made any payments
5 through June 30, 1999, the Staff believes that the Company's environmental reserve is
6 sufficient.

7 Q. Are there any pending data requests regarding the issue of environmental
8 costs?

9 A. Yes. Staff Data Request Nos. 118 and 121, which UE has objected to and
10 remain unanswered to date, concern questions about the Company's environmental
11 accruals both before and after the first sharing period of the second EARP. It is my
12 understanding that the Staff is utilizing the procedure set out in Commission Rule 4 CSR
13 240-2.090 (8) to attempt to obtain responses.

14 Q. What is the Staff's justification for proposing this adjustment?

15 A. The Staff cites sections 7.f.vi, 7.f.vii and 7.f.viii from the Case No.
16 EM-96-149 Stipulation and Agreement as previously quoted in this direct testimony. The
17 Staff believes that the Company's level of accrued environmental expense to be
18 excessive, especially in light of the fact that the Company has never made any actual
19 payments associated with these environmental costs to date. The Staff believes that this
20 condition represents a significant variation in expense with no reasonable explanation.
21 Considering that no actual cash payments have ever been made during any sharing period
22 of either the first or the second EARP, the Staff also believes that charging customers
23 with accrued levels of expenses represents a reduction in amounts to be shared by the

1 Company. Therefore, the Staff contends that making additional accruals for
2 environmental expenses represents a manipulation of earnings results as covered in the
3 Stipulation and Agreement. Also, the Staff is unaware of any prior rate proceeding,
4 involving UE, in which environmental accruals were at issue.

5 **INJURIES AND DAMAGES EXPENSE**

6 Q. Please explain injuries and damages expense.

7 A. Injuries and damages expense is based on maintaining a reserve of
8 accumulated funds to pay claims for injuries and damages that the Company anticipates
9 will be incurred, rather than amounts that are actually paid out. Accruals to increase the
10 reserve are expensed and actual claims are charged against the reserve balance when
11 paid. The reserve represents funds accumulated and set aside to pay claims for medical
12 costs, workmen compensation costs and lawsuits relating to injuries and damages. UE is
13 self-insured for these costs.

14 Q. What activity occurred with respect to injuries and damages during the
15 first sharing period of the second EARP?

16 A. During the first sharing period of the second EARP, the Company accrued
17 \$16,560,000 for injuries and damages. During the same period the Company made actual
18 payments of \$5,429,276. Based on this information, the Company has accrued over three
19 times more than the amount that was actually paid during the first sharing period of the
20 second EARP. In fact, in May 1999, the Company's total injuries and damages reserve
21 balance reached its highest level ever at \$26,966,591. By June 30, 1999, the ending point
22 of the first sharing period of the second EARP, the Company had an injury and damages
23 reserve balance of \$26,816,814. This level represents approximately a 70% increase in

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1 the reserve balance since the end of the previous sharing period, June 30, 1998. The
2 reserve balance at that date, \$15,686,089 was also an all-time high level. At the
3 beginning of the first EARP in June 1995, the Company had a total injuries and damages
4 reserve balance of \$12,910,843. This indicates that the Company's injuries and damages
5 reserve balance has increased by over \$13,900,000 since the inception of the first EARP.
6 This \$13,900,000 of additional injuries and damages reserve represents funds, the
7 majority of which, ratepayers have paid into the injuries and damages reserve, that have
8 not been paid out by the Company, since the beginning of the experimental alternative
9 regulation plans.

10 Q. Please explain the Staff's adjustment S-9.6 to injuries and damages.

11 A. The Staff calculated adjustment S-9.6 by subtracting the \$5,429,276 of
12 actual payments made by the Company during the first sharing period of the second
13 EARP from the Company's accrued level of \$16,560,000 during the same time period.
14 The result of this calculation produced a "gross adjustment" totaling \$11,130,724. The
15 Staff then applied an operation and maintenance expense factor as well as Missouri
16 electric and gas allocation factors to this gross adjustment level, which resulted in a final
17 adjustment of \$7,449,045. The Staff proposes to remove this \$7,449,045 of excess
18 accrual, which exceeds actual cash payments, in order to reflect injuries and damages
19 expense using a cash approach. The Staff's calculation for this adjustment is shown on
20 Schedule 3-1, which is attached to this direct testimony.

21 Q. Why does the Staff recommend a cash approach for the Company's
22 injuries and damages expense?

1 A. The Staff recommends a cash approach, for the Company's injuries and
2 damages expense in order to avoid the excess accrual which has resulted during the
3 current sharing period and which will continue to exist during future periods of the
4 second EARP. Additionally, the cash approach is based solely on actual cash payments
5 made during the period as opposed to the Company's accrual basis, which relies upon an
6 estimate of what actual future payments will be. As stated earlier in this testimony, the
7 Company accrued more than three times the level of actual cash payments during the
8 current sharing period. The Staff's adjustment is appropriate because it eliminates this
9 large over accrual situation and at the same time it reflects the actual injuries and
10 damages payments during this first sharing period of the second EARP.

11 Q. Are there any instances where a regulated Missouri utility is currently
12 using a cash approach to account for its injuries and damages expense for regulatory
13 purposes?

14 A. Yes. Laclede Gas Company and Missouri Gas Energy follow the Staff's
15 cash approach of accounting for injuries and damages expense for regulatory purposes.

16 Q. What explanation has the Company provided for its injuries and damages
17 accruals and why is this explanation unreasonable?

18 A. The Company indicates that it assesses its potential liability regarding
19 future payments for injuries and damages claims and bases its injuries and damages
20 accrual on this assessment. However, as has been previously discussed, the Company has
21 accrued more than three times the level of actual cash payments during the current
22 sharing period. Additionally, since the beginning of the alternative regulation plans, the
23 Company's injury and damages reserve has increased by over \$13,900,000. This clearly

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1 demonstrates the timing problem that exists with the Company's method of accruing for
2 injuries and damages.

3 Q. Are there any pending data requests regarding the issue of injuries and
4 damages?

5 A. Yes. Staff Data Request Nos. 120, 121, 123 and 124, which remain
6 unanswered to date, concern various matters related to injuries and damages.

7 Q. What is the Staff's justification for proposing this adjustment?

8 A. The Staff cites sections 7.f.vi and 7.f.vii from the Case No. EM-96-149
9 Stipulation and Agreement, as has been previously discussed in this direct testimony.
10 The Staff believes that the difference between accrued injuries and damages expenses and
11 actual injuries and damages payments is excessive and also represents a significant
12 variation in expense with no reasonable explanation. The Staff also believes that by
13 setting accrued levels of expense for injuries and damages at a level that is three times
14 more than actual cash payments represents a reduction to amounts to be shared with
15 customers. Therefore, the Staff believes that this action represents a manipulation of
16 earnings results as covered in the Stipulation and Agreement.

17 Q. Does this conclude your direct testimony?

18 A. Yes, it does.

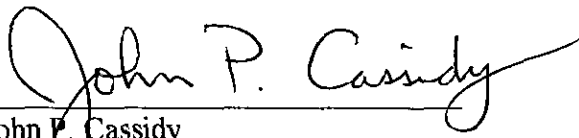
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

The Staff of the Missouri Public)	
Service Commission,)	Case No. EC-2000-795
)	
Complainant,)	
)	
v.)	
)	
Union Electric Company, d/b/a)	
AmerenUE,)	
)	
Respondent.)	

AFFIDAVIT OF JOHN P. CASSIDY

STATE OF MISSOURI)
) ss.
COUNTY OF ST. LOUIS)


John P. Cassidy, is, of lawful age, and on his oath states: that he has participated in the preparation of the foregoing Direct Testimony in question and answer form, consisting of 11 pages to be presented in the above case; that the answers in the foregoing Direct Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.



John P. Cassidy

Subscribed and sworn to before me this 30 day of May, 2000

GINGER L. HARRIS
Notary Public - Notary Seal
STATE OF MISSOURI
ST. LOUIS COUNTY
MY COMMISSION EXP. DEC. 17, 2002



Notary Public
My Commission Expires Dec. 17, 2002

RATE CASE PROCEEDING PARTICIPATION

JOHN P. CASSIDY

<u>COMPANY</u>	<u>CASE NO.</u>
Missouri Cities Water Company	WR-91-172
Missouri Cities Water Company	SR-91-174
St. Louis County Water Company	WR-91-361
Southwestern Bell Telephone Company	TC-93-224
Laclede Gas Company	GR-94-220
Empire District Electric Company	ER-95-279
Imperial Utility Corporation	SC-96-247
St. Louis County Water Company	WR-97-382
Laclede Gas Company	GR-98-374
United Water Missouri, Inc.	WR-99-326

UNION ELECTRIC COMPANY
EC-2000- 1st CREDIT PERIOD, 2nd EARP
LEGAL FEES

	<u>(Provision)</u> <u>Expense</u>	<u>(Charges)</u> <u>Payments</u>	<u>Annual</u> <u>Cumulative</u> <u>Excess</u> <u>Accrual</u>	<u>Credit Period</u> <u>Cumulative</u> <u>Excess</u> <u>Accrual</u>
1998				
January	87,000	156,798	(69,798)	
February	87,000	125,299	(108,097)	
March	87,000	411,861	(432,958)	
April	87,000	148,029	(493,987)	
May	87,000	372,080	(779,067)	
June	587,000	207,575	(399,642)	
July	87,000	133,028	(445,670)	(46,028)
August	87,000	323,191	(681,861)	(282,219)
September	1,087,000	347,389	57,750	457,392
October	87,000	274,827	(130,077)	269,565
November	87,000	223,775	(266,852)	132,790
December	87,000	131,730	(311,582)	88,060
Total	<u><u>2,544,000</u></u>	<u><u>2,855,582</u></u>	(311,582)	
1999				
January	250,000	81,377	168,623	256,683
February	250,000	139,117	279,506	367,566
March	250,000	100,405	429,101	517,161
April	250,000	147,668	531,433	619,493
May	250,000	144,697	636,736	724,796
June	250,000	339,624	547,113	635,173
July	250,000	181,314	615,799	
August	250,000	122,737	743,062	
September	250,000	144,001	849,061	
October	250,000	149,528	949,533	
November	250,000	235,423	964,110	
December	250,000	119,694	1,094,416	
Total	<u><u>3,000,000</u></u>	<u><u>1,905,584</u></u>	1,094,416	
July 1998 - June 1999	3,022,000	2,386,827	635,173	
Missouri Electric Factor	<u>88.59%</u>	<u>88.59%</u>	<u>88.59%</u>	
Missouri Electric O & M	<u><u>2,677,190</u></u>	<u><u>2,114,490</u></u>	<u><u>562,699</u></u>	

UNION ELECTRIC COMPANY
EC-2000- 1st CREDIT PERIOD, 2nd EARP
INJURIES AND DAMAGES

	<u>Reference</u>	<u>Beginning Of Year Balance</u>	<u>(Provision) Expense</u>	<u>(Charges) Payments</u>	<u>Ending Balance</u>
June 30, 1998	F&S p. A 4-2	11,383,805	16,300,000	(11,997,716)	15,686,089
December 31, 1998	F&S p. A 4-2	11,383,805	27,300,000	(13,739,343)	24,944,462
June 30, 1999	F&S p. A 4-2	24,944,463	<u>5,560,000</u>	<u>(3,687,649)</u>	26,816,814
Total During Period			16,560,000	<u>(5,429,276)</u>	
Payments During Period			<u>5,429,276</u>		
Gross Adjustment			11,130,724		
O & M Factor	Note 1		<u>78.09%</u>		
O & M Portion			8,691,802		
Gas Allocation @ 3.026%			<u>283,353</u>		
O & M Electric			8,408,449		
Missouri Electric Factor			<u>88.59%</u>		
Missouri Electric O & M			<u>7,449,045</u>		
Note 1:					
F & S B2-1a	<u>Total</u>	<u>Construction Transfers</u>	<u>O&M</u>		
Year to date 6/30/98	17,143,735	(1,441,215)	15,702,520		
Year to date 12/31/98	28,625,076	(3,610,577)	25,014,499		
Year to date 6/30/99	8,416,111	(2,190,493)	6,225,618		
Total	<u>19,897,452</u>	<u>(4,359,855)</u>	<u>15,537,597</u>		
Percentage	100.00%	-21.91%	78.09%		