

Exhibit No.:
Issue: Income Taxes
Witness: Gregory L. Nelson
Type of Exhibit: Supplemental Surrebuttal
Testimony
Sponsoring Party: Union Electric Company
Case No: EO-96-14

MISSOURI PUBLIC SERVICE COMMISSION

Case No. EO-96-14

FILED

JUN 3 1999

Missouri Public
Service Commission

SUPPLEMENTAL SURREBUTTAL TESTIMONY

OF

GREGORY L. NELSON

ST. LOUIS, MISSOURI
June, 1999

1 **Supplemental Surrebuttal Testimony of Gregory L. Nelson**
2 **Vice President and Tax Counsel**
3 **MPSC Case No. EO-96-14**
4

5 **Q. Please state your name and business address.**

6 A. My name is Gregory L. Nelson, and my business address is 1901
7 Chouteau Avenue, St. Louis, Missouri, 63103.

8 **Q. Are you the same Gregory L. Nelson who previously filed**
9 **supplemental rebuttal testimony in this case?**

10 A. Yes, I am.

11 **Purpose of Testimony**

12 **Q. What is the purpose of your supplemental surrebuttal testimony in**
13 **this proceeding?**

14 A. The purpose of this supplemental surrebuttal testimony is to supplement
15 my own supplemental rebuttal testimony concerning Staff's proposed deduction of the
16 debt component of the allowance for funds used during construction ("AFUDC-debt") in
17 computing the current tax expense of Union Electric Company ("Company") in this
18 proceeding.

19 **Adjustment for AFUDC-Debt**
20

21 **Q. In your supplemental rebuttal testimony, did you address an**
22 **adjustment concerning AFUDC-debt proposed by Commission Staff witness Steven**
23 **Rackers?**

24 A. Yes, at page 2, line 16 through page 9, line 10, I addressed Mr. Rackers'
25 proposal to include AFUDC-debt as a deduction in the calculation of current income tax
26 expense.

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1 **Q. What conclusion did you reach?**

2 A. I concluded that Mr. Rackers' proposed adjustment was erroneous.

3 **Q. Do you continue to believe that the adjustment is erroneous?**

4 A. No, Mr. Rackers' proposed adjustment is correct.

5 **Q. What is the basis for your conclusion that Mr. Rackers' proposed**
6 **adjustment is correct?**

7 A. The analysis that I presented in my supplemental rebuttal testimony
8 reflected the calculation of current tax expense that is used in the Company's actual tax
9 return and for book purposes (the "tax/book calculation"). I met with Mr. Rackers after
10 filing my supplemental rebuttal testimony and, during that meeting, I learned that the
11 Commission requires a different method to calculate current tax expense for regulatory
12 purposes (the "regulatory calculation").

13 The tax/book calculation includes as a nonoperating item a deduction for all
14 actual interest (including AFUDC-debt). In contrast, the regulatory calculation contains
15 as nonoperating items separate deductions for (i) the interest on ratebase allowed for
16 regulatory purposes measured by the weighted cost of debt times ratebase, and (ii)
17 AFUDC-debt. Thus, AFUDC-debt is a nonoperating deduction in both the tax/book
18 calculation and in the regulatory calculation. In both calculations, a separate
19 nonoperating item reverses the AFUDC-debt deduction in computing pre-tax book
20 income, and Schedule M items are provided for AFUDC-debt and for interest that is
21 capitalized for tax purposes. In both calculations, deferred taxes are computed using
22 those Schedule M items.

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My analysis of Mr. Rackers' proposed adjustment was correct in the context of the tax/book calculation described in my supplemental surrebuttal (*i.e.*, the proposed adjustment would have resulted in a double deduction of AFUDC-debt). However, in the regulatory calculation, Mr. Rackers' deduction of AFUDC-debt does not result in a double deduction and is therefore appropriate.

Q. Using the assumptions set forth in your example at page 5, lines 19-29 and assuming further that there is \$30 of regulatory interest and no short-term interest, explain the regulatory calculation.

A. The first step is to compute pre-tax book income:

Operating income:	\$100
Plus: AFUDC (debt and equity) income	20
Minus: regulatory interest on ratebase	(30)
Minus: AFUDC-debt	<u>(10)</u>
Equals: Pre-tax book income	\$80

The second step is to compute taxable income. To do this, the Company would make two Schedule M adjustments to pre-tax book income.

Pre-tax book income	\$80
Minus: Schedule M item to remove AFUDC (debt and equity)	(20)
Plus: Schedule M item to reverse the book interest deduction for the portion of interest that is capitalized for tax purposes	<u>8</u>
Equals: Taxable income	68

The final step is to compute the tax:

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1	Taxable income	\$68
2	Times: tax rate	<u>40%</u>
3	Equals: current income tax	\$27.2

4 **Q. What comprises the \$4 difference between the \$27.2 current tax**
5 **expense in your example, above and the \$23.2 current tax expense, computed at**
6 **page 7, line 7 of your supplemental rebuttal testimony?**

7 A. This \$4 difference is attributable to the \$10 difference between actual and
8 regulatory interest on ratebase, times the 40% assumed income tax rate.

9 **Q. State your conclusion in terms of the actual amounts associated with**
10 **this issue?**

11 A. The AFUDC-debt that should be deducted in the regulatory calculation
12 (the \$10 in the example) is \$2,538,459.

13 **Q. Are any changes to the Company's deferred taxes associated with**
14 **AFUDC-debt necessary as a result of Mr. Rackers' adjustment?**

15 A. No.

16 **Q. Does this conclude your supplemental surrebuttal testimony?**

17 A. Yes, it does.

MISSOURI PUBLIC SERVICE COMMISSION

STATE OF MISSOURI

In the Matter of the Monitoring of the)
Experimental Alternative Regulation Plan of) Case No. EO-96-14
Union Electric Company)

AFFIDAVIT OF GREGORY L. NELSON

FILED

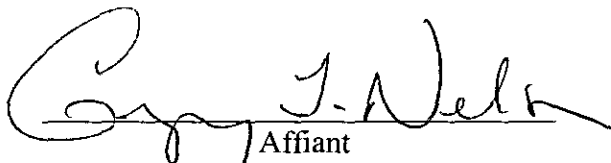
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CITY OF ST. LOUIS)

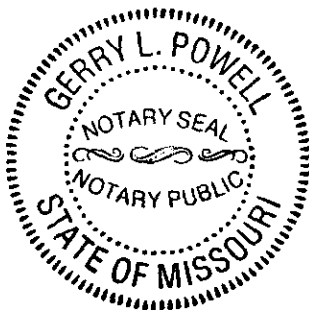
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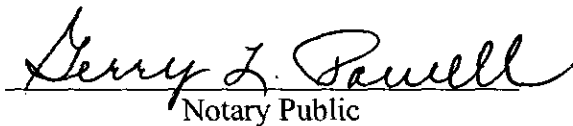
Gregory L. Nelson, being first duly sworn on his oath, states:

1. My name is Gregory L. Nelson. I work in the City of St. Louis, Missouri, and I am the Vice President and Tax Counsel of Ameren Services Company.
2. Attached hereto and made a part hereof for all purposes is my Supplemental Surrebuttal Testimony consisting of pages 1 through 4, all of which has been prepared in written form for introduction into evidence in Missouri Public Service Commission Case No. EO-96-14.
3. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded are true and correct.


Affiant

Subscribed and sworn to before me this 2nd day of June, 1999.




Notary Public

