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October 23, 2000

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FILED³

OCT 23 2000

Missouri Public
Service Commission

Mr. Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge
Missouri Public Service Commission
P. O. Box 360
Jefferson City, MO 65102

RE: Case No. EM-96-149 – In the Matter of the Application of Union Electric Company for an Order Authorizing: (1) Certain Merger Transactions Involving Union Electric Company; (2) The Transfer of Certain Assets, Real Estate, Leased Property, Easements and Contractual Agreements to Central Illinois Public Service Company; and (3) In Connection Therewith, Certain Other Related Transactions.

Dear Mr. Roberts:

Enclosed for filing in the above-captioned case are an original and eight (8) conformed copies of **STAFF'S SUGGESTIONS IN SUPPORT OF THE STIPULATION AND AGREEMENT RESPECTING THE SHARING CREDITS OF THE FIRST YEAR OF THE SECOND UE EXPERIMENTAL ALTERNATIVE REGULATION PLAN.**

This filing has been mailed or hand-delivered this date to all counsel of record.

Thank you for your attention to this matter.

Sincerely yours,

Steven Dottheim
Chief Deputy General Counsel
(573) 751-7489
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Enclosure
cc: Counsel of Record

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

FILED³

OCT 23 2000

Missouri Public
Service Commission

In the Matter of the Application of Union Electric Company)
for an Order Authorizing: (1) Certain Merger Transactions)
Involving Union Electric Company; (2) The Transfer of)
Certain Assets, Real Estate, Leased Property, Easements)
and Contractual Agreements to Central Illinois Public)
Service Company; and (3) In Connection Therewith,)
Certain Other Related Transactions.)

Case No. EM-96-149

**STAFF'S SUGGESTIONS IN SUPPORT OF THE STIPULATION AND AGREEMENT
RESPECTING THE SHARING CREDITS OF THE FIRST YEAR OF THE SECOND
UE EXPERIMENTAL ALTERNATIVE REGULATION PLAN**

Comes now the Staff of the Missouri Public Service Commission (Staff) in support of the Stipulation And Agreement respecting the sharing credits of the first year of the second Union Electric Company (UE) experimental alternative regulation plan (EARP). On August 25, 2000, the Staff, the Office of the Public Counsel (Public Counsel) and UE filed a Stipulation And Agreement entered into by them respecting the sharing credits of the first year of the second EARP. In support of that Stipulation And Agreement, the Staff states as follows:

1. The Staff adjustments filed on May 30, 2000 were sponsored by Staff witnesses, John Cassidy, John Boczkiewicz and Stephen Rackers. As filed on May 30, 2000, the Staff adjustments result in a calculation of return on common equity (ROE) for UE of 13.949% for the period in question, which places UE at the 50% sharing level of the sharing grid in Case No. EM-96-149 for all of the Staff's adjustments when considered alone of the Public Counsel's adjustments. The UE sharing grid in Case No. EM-96-149 provides for (1) 100% of UE's earnings up to and including a 12.61% ROE going to UE alone; (2) a 50% sharing between

ratepayers and UE of that portion of UE's earnings greater than a 12.61% ROE to and including a 14.00% ROE; (3) 90% of UE's earnings greater than a 14.00% ROE up to and including a 16.00% ROE going to ratepayers and 10% going to UE; and (4) 100% of UE's earnings greater than a 16.00% ROE going to ratepayers alone. Adding the Public Counsel's adjustments filed on May 30, 2000 to the Staff's adjustments, results in a calculation of UE's ROE of 13.979%, which still places UE at the 50% sharing level of the sharing grid in Case No. EM-96-149. (The dollar amount of the terms of the Staff's settlement with UE causes UE's ROE to be 13.717% for the period in question. Adding the dollar amount of the terms of Public Counsel's settlement with UE to the dollar amount of the terms of the Staff's settlement with UE causes UE's ROE to be 13.746% for the period in question.).

The sharing grid for the second EARP is as follows:

SECOND EARP – Case No. EM-96-149			
Earnings Level (Missouri Retail Electric Operations)		Sharing Level	
		UE	Ratepayer
1	Up to and including 12.61% ROE	100%	0%
2	That portion of earnings greater than 12.61% up to and including 14.00% ROE	50%	50%
3	That portion of earnings greater than 14.00% up to and including 16.00% ROE	10%	90%
4	That portion of earnings greater than 16.00% ROE	0%	100%

If the amount at issue for a particular issue caused UE to be at the 90% sharing level of the sharing grid rather than at the 50% sharing level of the sharing grid, the sharing credit value to ratepayers of that portion of any of the following issues would be 1.8 times the value shown below. Since prior to settlement the amount at issue between the Staff and UE

caused UE to be at the 50% level of the sharing grid, the dollar value for any Staff issue shown below quantified as a sharing credit is 50% of what the dollar value of that Staff adjustment would be in a rate increase or an excess earnings complaint case.

Issue	Staff Adj. As Filed: Credit Amt. To Go To Ratepayers	Staff Adj. As Settled: Credit Amt. To Go To Ratepayers	Staff Witness	Staff Rationale (EM-96-149 Stip. & Agreement, ER-95-411 Stip. & Agreement, EO-96-14 R. & Order)
Environmental Accrual	\$1.000 M	\$1.000 M	Cassidy	7.f.vi., 7.f.vii., 7.f.viii. in EM-96-149 Stip. & Agreement
Targeted Separation Plan	\$2.734 M	\$2.734 M	Boczkievicz	7.f.viii.
Advertising Expense	\$0.551 M	*	Boczkievicz	7.f.vi., 7.f.vii., Att.C-2.g.
Legal Expense ¹	\$0.285 M	*	Cassidy	7.f.vi., 7.f.vii., 7.f.viii.
Territorial Agreements	\$0.542 M	*	Rackers	12/23/99 R. & Order in EO-96-14 (3.f.vii., 3.f.viii. in ER-95-411 Stip. & Agreement) – 7.f.vii., 7.f.viii., 7.h.
* Advertising Expense, Legal Expense and Territorial Agreements Settlement Amount		\$1.000 M		
Injuries And Damages	\$3.778 M	\$0.000	Cassidy	7.f.vi., 7.f.vii.
Income Taxes			Rackers	
TOTAL	\$8.890 M	\$4.734 M		

7.f.vi.: earnings manipulation

7.f.vii. (also 3.f.vii.): issues which cannot be resolved by the signatories, including significant variations in the level of expenses associated with any category of cost, where no reasonable explanation has been provided

7.f.viii. (also 3.f.viii.): concerns over any category of cost that has been included in UE's monitoring results and has not been included previously in any ratemaking proceeding

Att. C-2.g. (Attachment C, Section 2.g.): issues relating to the operation or implementation of the EARP

¹ Based on additional information received by the Staff from UE after the Staff filed its direct testimony on May 30, 2000, the Staff revised the amount of the sharing credit to ratepayers upward from \$.285 million to \$.466 million.

Regarding income taxes, the direct testimony of Stephen Rackers filed on May 30, 2000 noted that the Staff believed that this area of concern had been resolved by the Staff and UE. On June 9, 2000, UE filed a Corrected Final Earnings Report based upon items identified by the Staff with respect to UE's calculation of income taxes. With these revisions by UE, the Staff considers the income taxes area resolved.

2. UE's corrected final earnings report shows a sharing credit for the first period of the second EARP of \$14.9 million to go to ratepayers. The sharing credit filed by the Staff on May 30, 2000 for the first period of the second EARP amounted to \$23.8 million to go to ratepayers. Of the approximately \$9.0 million that remained at issue between the Staff and UE, the Staff and UE reached an agreement that results in the amount of the sharing credit to go to ratepayers being increased by \$4.734 million from UE's proposed \$14.9 million. The Public Counsel settled the three issues that it had with UE, resulting in an increase of the sharing credit to go to ratepayers by \$.525 million. In reaching a total dollar settlement with UE and Public Counsel in the amount of a \$20.214 million sharing credit to go to ratepayers, the Staff considered (a) the Commission's decisions respecting the issues that went to hearing regarding the prior sharing credit period, (b) the time value of money and the length of the time involved in going to hearing and possible judicial review versus settling and getting credits to ratepayers sooner than would otherwise be the case and (c) the amount of dollars and the significance of the principles at stake respecting the unresolved issues. Based on these considerations, the Staff believes that the settlement reached is reasonable.

3. The Staff and Company agreed as is indicated below respecting the Staff's adjustments filed on May 30, 2000. The Staff has no objection to the terms of the settlement of the Public Counsel's adjustments. As related in the Stipulation And Agreement filed with the

Commission on August 25, 2000, the adjustments listed below are agreed to by the signatories to this Stipulation And Agreement for this particular sharing period only, except as noted concerning Income Taxes and the Targeted Separation Plan. For purposes of understanding the operation of the experimental alternative regulation plan, again it should be stated that since the amount at issue between the Staff and UE, prior to the settlement, caused UE to be at the 50% level of the sharing grid, the dollar value for any Staff issue shown below quantified as a sharing credit is 50% of what the dollar value of that Staff adjustment would be in a rate increase or an excess earnings complaint case.

- a. Environmental Accrual – Before the sharing period which is the subject of the instant review (the first sharing period of the second EARP), the Company had accrued approximately \$3,887,065 as a reserve for environmental costs and had never paid any amount out of this accrual. During the sharing period under review, the Company accrued approximately an additional \$2,000,000 for environmental expenses that it contended it might incur in the future. During the sharing period, the Company did not pay any environmental costs. The Company agrees to remove \$2,000,000 from expense for the sharing period.
- b. Targeted Separation Plan (TSP) – Ameren in March 1998 announced plans to reduce operating expenses, including plans to eliminate approximately 400 employee positions by mid-1999 through a hiring freeze and the TSP. During the third quarter of 1998, the Company recorded a nonrecurring charge of nearly \$18,000,000 representing the cost to implement TSP. Approximately \$11,000,000 of expense savings were actually realized during the sharing period. The Staff does not seek to disallow any costs, but simply to match the amounts of costs incurred with the actual savings realized during the particular sharing period. The Company agrees to defer inclusion of \$5,468,000 of the cost of the TSP until the next sharing period. The Staff agrees that this amount will in fact be included as an expense in the Staff's calculation of the Company's ROE for the second sharing period of the second EARP.
- c. Injuries and Damages – During the sharing period, the Company accrued \$16,560,000 for injuries and damages, in addition to the balance of past accruals in the injuries and damages reserve, and made actual payments of \$5,429,276. At the end of the sharing period, the Company had an injury and damages reserve balance of \$26,816,814, which was approximately a 70% increase in the reserve balance since the end of the previous sharing period. The Missouri jurisdictional expense portion of the difference between the amount accrued and the amount of actual payments results in

an adjustment of \$7,449,045. The Staff agrees not to pursue an adjustment in this area for the first sharing period of the second EARP.

- d. Legal Accrual, Advertising and Territorial Agreements – The Staff agrees not to pursue an adjustment in each of these areas for the instant first sharing period of the second EARP and the Company agrees to increase the amount of the sharing credits to be received by ratepayers by \$1,000,000 as a result.
 - i. Legal Accrual – The Staff's adjustment as filed removed \$562,699 of what the Staff asserts is excess accrual over actual payments, in order to treat legal fees under a cash approach. For the sharing period, the Company accrued for Missouri electric operations approximately \$2,677,190 in legal fees, however the Company actually paid \$2,114,490 for legal fees during the same period.
 - ii. Advertising – The Staff classified \$1,337,231 of the Company's advertising as institutional advertising and removed this amount of expense from the Staff's calculation of sharing credits. Institutional (goodwill) advertising is designed to enhance the Company's public image and is not necessary for the provision of safe and adequate service.
 - iii. Territorial Agreements – The Staff adjustment of approximately \$1,100,000 reversed the effect on earnings related to separate territorial agreements between (1) UE and Black River Electric Cooperative and (2) UE and Macon Electric Cooperative. In each instance, the Company realized a net loss of customers and associated revenues from the exchange of a portion of its service area with that of the two cooperatives. This specific adjustment was approved by the Commission for the third sharing period of the first EARP, which was contested before the Commission in the immediately preceding credit period.
- e. Income Taxes – The Company accepted Staff adjustments respecting Income Taxes as corrections to the Company's calculation consistent with the Case No. EM-96-149 Stipulation And Agreement. The Company had already agreed to adjust its sharing calculation for the first sharing period of the second EARP irrespective of the settlement discussions that led to the Stipulation And Agreement filed on August 25, 2000. As part of the complete resolution of the sharing credits issues for the first sharing period of the second EARP, the Company agrees that the revisions reflected in the calculation of Income Taxes that it filed on June 9, 2000 also will apply to the calculation of Income Taxes for the second and third sharing periods of the second EARP.

With respect to the adjustments recommended by OPC, UE agreed to proceed as follows and the Staff has no objection:

- f. Strategic planning cost – The Company will accept this adjustment of \$978,913 to its earnings calculation.

- g. Genco Operating Model – The Company will accept an adjustment of \$70,678 to its earnings calculation.

4. The Staff's rationale for entering into the Stipulation And Agreement filed on August 25, 2000 is solely its own and is being provided for the purpose of advising the Commission how the Staff arrived at the settlement number and why the Staff believes that the Commission should approve the Stipulation And Agreement. Given the fact that UE could litigate the outstanding issues, seek judicial review of any Commission decision with which it disagrees and seek a suspension or stay of such Commission decision, the Staff views the settlement as comprising an equitable resolution of the Staff's and UE's positions with neither party conceding anything respecting the position of the other. With Commission acceptance of the instant Stipulation And Agreement, only the second and third sharing periods of the second EARP will remain for resolution and the second year of the second EARP concluded June 30, 2000.

5. The Staff would note that Section 7.g. of the Stipulation And Agreement in Case No. EM-96-149 provides that "[b]y February 1, 2001, UE, Staff and OPC will file, and other signatories may file their recommendations with the Commission as to whether the New Plan should be continued as is, continued with changes (including new rates, if recommended) or discontinued." Thus, the Staff is concerned with a proper monitoring and calculation of sharing credits for the second and third sharing periods of the second EARP, and, in addition, the Staff is focusing on the February 1, 2001 filing that is required to be made with the Commission respecting the second EARP and what should follow upon the conclusion of the second EARP.

Wherefore the Staff requests that the Commission approve the Stipulation And Agreement filed by the Staff, Public Counsel and UE on August 25, 2000 resolving all outstanding issues respecting the sharing credits for the first year of the second UE EARP.

Respectfully submitted,

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Certificate of Service

I hereby certify that copies of the foregoing have been mailed, hand-delivered or sent by facsimile transmission to all counsel of record as shown on the attached service list this 23rd day of October 2000.



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