BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Union Electric Company d/b/a AmerenUE for Authority to File Tariffs Increasing Rates for Electric Service Provided to Customers in the Company's Missouri Service Area.	)))))	Case No. ER-2010-0036

REPLY BRIEF OF AMERENUE

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INTRODUCTION

The record in this case shows that AmerenUE consistently provides its customers with high quality and reliable service at very competitive rates, an aspect of this case that the other parties in this case choose to ignore in their testimony and briefs. In particular:

- AmerenUE's system reliability has improved and currently ranks in the first quartile for reliability.[1]
- The Company's equivalent availability for its coal-fired power plants is very high at approximately 89%.[2]
- AmerenUE's storm restoration practices have been widely praised by Staff and others, including most recently with regard to its response to the devastating ice storm that struck Southeast Missouri in January, 2009.[3]
- AmerenUE has continued to aggressively invest in its system, investing more than $650 million in capital improvements just since September 30, 2008, the cut-off for known and measurable changes for AmerenUE's last rate case. All of these capital improvements have been serving AmerenUE's customers for some time; none of them have been reflected in rates.[4]
- No party has alleged any imprudence in AmerenUE's operations in this rate case.
- AmerenUE's rates are the lowest among investor-owned utilities in the state, and even at the level originally requested in this case, would have remained approximately 30% below the national average.[5]

[1] Tr. p. 915, l. 4-6.
[2] Tr. p. 943, l. 11-15.
[3] Ex. 109, p. 15, l. 14-16; (Wakeman rebuttal); Ex. 110, p. 6, l. 18-22 (Wakeman surrebuttal).
[4] Tr. p. 870, l. 4-7.
[5] Ex. 100, p. 5, l. 23 to p. 6, l. 9.

- AmerenUE is doing its part to control costs. It reduced certain costs originally planned for 2009, cut approximately $1 billion of expenditures that were originally part of its five-year plan developed in early 2009, instituted voluntary and involuntary separation programs, and has frozen management salaries.[6]

At the same AmerenUE was providing high quality service, the record also clearly shows that AmerenUE was consistently unable to recover its costs and earn anywhere close to its authorized return on equity over the last several years, as outlined at pages 1 to 3 of the Company's Initial Brief.

The positions set forth by the Staff, OPC and MIEC, if adopted, would materially and detrimentally aggravate this situation to the detriment of both the Company and its customers. As addressed in detail at pages 3 through 7 of the Company's Initial Brief, they have advocated unsupported, unreasonable, and punitive adjustments to the Company's cost of service that would make it even less likely that the Company will have any real chance to recover its costs and earn a reasonable return.[7]

Not only do these positions unfairly and unlawfully deprive AmerenUE of any real opportunity to recover its costs and earn a reasonable return, but adoption of them would also be detrimental to our customers because they would limit AmerenUE's ability to continue investing in its system beyond the minimum level of investment necessary to meet its statutory obligation

[6] Ex. 101, p. 11, l. 22 to p. 12, l. 25 (Baxter rebuttal).

[7] The Staff's Initial Brief contains a somewhat extended recitation of excerpts from prior court cases about the role of the Commission. Common among almost all of those excerpts is the duty to ensure that there exists "substantial justice between patrons and public utilities." The Staff cites one out-of-context statement which accurately states that the principal reason the Public Service Commission Act itself was *enacted* was to protect the public from what had previously been "destructive competition (i.e., costly duplication of facilities) and of course private utilities more than a century ago serving only the customers that were easiest and cheapest to serve. But another key facet of creating the Commission was to create a body "equipped with experts, technical knowledge, and other efficient aids to a ***neutral and full investigation*** . . ." of the matters before it. *Barker* (cited by the Staff in footnote 8), 163 S.W. at 860. An ROE recommendation that is 124 basis points below the national average; hiring consumer advocate experts, and proposing depreciation rates at the 20th percentile using methodologies no one else uses, etc. hardly evidence a Staff committed to a "neutral and full" investigation. To the contrary, these positions, and the Staff's suggestion that the revenue requirement be based on factors other than cost of service, suggest that the Staff is improperly assuming the role of consumer advocate. That's OPC's job; that's MIEC's job for its clients; that's the Missouri Retailers Associations' job for its clients, but it is most certainly not the Staff's job, nor is it a proper role for employees of a body whose duty is to conduct a neutral investigation.

to provide its customers with "safe and adequate" service, and would undermine the Company's ability to deliver the high level of service its customers expect. As AmerenUE CEO Warner Baxter testified:

> Should the Commission adopt the "out of the mainstream" positions, and/or the aggressive normalization proposals advocated by these parties, there would be meaningful negative implications. In particular, the excessive regulatory lag which I described in my previous testimonies would only be aggravated further. Consequently, the related negative policy implications of excessive regulatory lag would clearly become worse. The rates that the Commission would establish would not provide us with a reasonable opportunity to recover our prudently incurred costs of providing service, as well as a reasonable opportunity for our shareholders to earn a fair return on their investment. In addition, our already existing negative free cash flows would materially increase. Consequently, our credit quality, financing costs and ability to access the capital markets at reasonable rates would be negatively impacted. Finally, not only would adoption of these positions create a strong disincentive for us to pursue any new investments to meet customer expectations or strongly support state and federal policies and initiatives, we would be left with no reasonable choice but to meaningfully reduce our level of investment in our energy infrastructure and in our operations, consistent with the cash flows we derive from this rate case. This reduced investment would weaken the reliability of our distribution system and power plants, result in job losses, further weaken the economy of our communities and the state, and ultimately harm our customers.[8]

Mr. Baxter wasn't the only witness in this case to express concern about ROEs and depreciation rates that are too low. Office of the Public Counsel (OPC) witness Daniel Lawton pointed out that returns that are too low, depreciation expense that is too low, and fuel adjustment clauses that don't "recover your actual expenditure cost, absent imprudence," are all problematic.[9]

The Commission should not adopt the unreasonable and punitive revenue requirement positions advocated by Staff, MIEC and OPC in this case. Instead, it should adopt the positions on these issues advocated by the Company, which are in fact supported by sound principles of public utility ratemaking and, just as importantly, are supported by competent and substantial evidence *of record* in this case. Adoption of the Company's positions is necessary if the

[8] Ex. 101, p. 3, l. 8-29 (Baxter rebuttal).
[9] Tr. p. 2236, l. 24 to p. 2238, l. 14.

Company is going to have the cash flows it needs to cover its legitimate depreciation expense, to invest in its system as its customers expect it to do, and if the Company is to have any reasonable opportunity to recover its other operating costs and earn a fair return on its investment.

Before turning to each of the remaining contested issues in this case we must also address the hyperbole that is replete in the introductory portions of both the Staff's and the MIEC's Initial Briefs. The overriding theme of the introduction to the Staff's Initial Brief is that during any tough economic period, it is somehow illegitimate for a public utility with its long-term, ongoing obligation to serve, to ask for a rate increase that fully covers its costs; that provides it the cash flows it needs; and that hopefully will give it a reasonable opportunity to earn a fair return.[10] To the contrary, the Company has to provide service, and can raise its prices only with the Commission's permission, which is why this case exists in the first place.

Staff criticizes the Company for not proposing a phase-in of rates. Not only did not a single party propose a phase-in, but given how rates are set, a phase-in would, by definition, amount to a disallowance of part of the revenue requirement the Commission would have found in this case to be *necessary* to provide the Company with a reasonable opportunity to earn a fair return.[11]

The Staff also points to the public hearings and the public testimony about the financial burden certain low-income customers may face with a rate increase. In addition, the Staff encourages the Commission to "not blind" itself to the current state of the economy.

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[10] But unlike entities like the members of MIEC, the Company cannot idle or cut back on the shifts at a beer or seed production or drug manufacturing facility during difficult economic periods, and it can't raise its prices to the extent the market will bear it. MIEC's introduction suggests a role for the Commission it cannot assume as a matter of law, and does so by citing to statistics that are not a part of the record in this case. Consequently, the Commission cannot rely on MIEC's arguments or these extra-record sources of information. We would also note that there is no indication whatsoever that the "closures of major plants" has anything whatsoever to do with electric rates in Missouri, least of all the comparatively low industrial rates charged by AmerenUE.

[11] We would note that the Staff, which is ordinarily extremely sensitive itself to any attempt to use prior Stipulations and Agreements as precedent in other proceedings, is violating the Stipulation and Agreement *it signed* and the Commission approved by in effect citing as precedent an *agreed-upon* rate decrease phase-in in Case No. EC-2002-1.

As noted earlier, AmerenUE has an obligation to serve. Its current rates do not cover its costs and do not provide it a reasonable opportunity to earn a fair ROE. While the social problems relating to the ability of low-income customers to pay a host of expenses, only one of which is their electric bill, is not a matter that this Commission or the Company can solve,[12] AmerenUE has recognized the plight of its Company's low-income customers[13] and has taken steps where it can to address these problems by actively participating in setting policies and in finding solutions to assist these customers.[14] On top of these many steps, in a settlement filed in this case (which was to resolve all issues related to low-income customers), AmerenUE agreed to fund, along with our customers, a pilot program that is targeted to assist its low-income customers.[15]

The Commission may, through rate design, have some ability to address low-income issues, but shifting costs from residential customers to other customer classes was met with objection from the industrial intervenors in this case. As MIEC witness Maurice Brubaker testified about the possibility of establishing low-income rates, "[g]iven the lack of availability of reliable information, the absence of any specific proposal, and the broad ranging and potentially open-ended nature of the financial impact, there is nothing before the Commission for approval that can be acted upon."[16]

[12] The problems of poverty, lack of education, etc. are matters that if they are to be addressed by government, they must be addressed by the Legislature.
[13] Ex. 138, p. 2, l. 9-19 (Mark direct).
[14] *Id.* p. 2, l. 22 to p. 3, l. 9, 14-16. These efforts include participation in the 2009 Missourians to End Poverty Summit, leadership roles in the monthly meetings for the Community to Keep Missourians Warm, and active involvement in the Edison Electric Institute's Low Income Energy Issues group and the National Fuels Fund group, both of which are national programs to address these very issues. AmerenUE also currently assists customers through our Dollar More Program and our low-income weatherization contributions, has offered its Clean Slate program to remove customer arrearages and offers budget billing to all customers to smooth the variability of their energy bills as well as funding the Meet the Heat and Be Cool programs.
[15] The Commission approved the agreement.
[16] Ex. 414, p. 5, l. 5-8 (Brubaker rebuttal on low income).

I. RETURN ON EQUITY.

A. Staff witness David Murray's extremely low recommended ROE is based on unconventional and inappropriate analyses and must be rejected.

As explained in detail in the Company's Initial Brief, Mr. Murray's ROE recommendation of 9.35% is completely inappropriate. Nothing in Staff's Initial Brief can disguise the many shortcomings in Mr. Murray's analysis that have led him to recommend an ROE 124 basis points below the national average for integrated electric utilities, and dozens of basis points below the very lowest ROEs authorized anywhere for any electric utility under any circumstances over the past several years.[17] Mr. Murray's recommended ROE is irresponsibly low, his analysis is fundamentally flawed, and the Staff's Initial Brief provides no explanation that would justify the Commission giving that recommendation any consideration in setting AmerenUE's ROE.

Staff's Initial Brief states that Mr. Murray's recommendation "is influenced by the results of various 'traditional' cost of capital methodologies, including the Capital Asset Pricing Model (CAPM), the constant-growth discounted cash flow methodology (constant-growth DCF) and the multi-stage discounted cash flow methodology (multi-stage DCF)."[18] Actually nothing could be further from the truth. As Mr. Murray testified, the range for his ROE recommendation (and his midpoint recommendation) were developed *exclusively* through the use of his multi-stage DCF,[19] which produced a 9.2% ROE. Mr. Murray testified:

> Q. Now, in terms of how you developed your recommended cost of equity, my understanding is that you established your range based on the results of your multistage discounted cash flow or DCF analysis; is that correct?

[17] Mr. Murray's recommended ROE is also 75 basis points below the midpoint recommendation of the Office of the Public Counsel, the advocate on behalf of the public in Missouri rate cases.
[18] Staff's Initial Brief, pp. 16-17.
[19] The constant-growth DCF, not the multi-stage DCF is the method most commonly used by this Commission and others in setting ROEs for utilities. Tr. p. 1961, l. 22-25. Staff admits in its brief that multi-stage methodologies "are generally reserved for industries in the early stages of a growth cycle." Staff's Initial Brief, p. 27. And of course they tend to produce lower ROEs than the traditional constant growth DCF.

A. *That's correct.*

Q. And my further understanding is that when you performed your multistage DCF analysis, you got a cost of equity of 9.2 percent from that analysis; is that correct?

A. *That was the midpoint, yes.*

Q. And then my understanding is that you initially put a band of 50 basis points on either side of that 9.2 percent cost estimate?

A. *Yes.*

Q. And then—but then you—and that gave you a range of 8.7 to 9.7, correct?

A. *Yes.*

Q. But then you truncated the bottom half of the range at 9 percent—

A. *Yes.*

Q. --is that right? And why did you do that?

A. *That was one of those considerations about, although I believe there's information that supports a cost of equity in the high 8's, and I believe I've provided that from the investment community, one of the things that I considered is obviously there's a belief from this Commission that I may be—or at least certain Commissioners, that that may be too low, and—and so I took that into consideration in adopting a recommended range of 9 to 9.7.*

I think if somebody sees an 8, it frightens them. It cannot be possible. *Based on my review of various folks that make investment decisions, it's quite possible, but I understand that, you know (emphasis* ***in bold****).*[20]

No results other than the multi-stage DCF results were included in Mr. Murray's calculation of his range or midpoint, which is one of the many flaws in his analysis.[21]

The second major flaw in Mr. Murray's analysis is that he used an unusual and inappropriate growth rate in his multi-stage DCF model. Specifically, he used growth in

[20] Tr. p. 2030, l. 7 to p. 2031, l. 17.

[21] Mr. Gorman testified that he is in agreement with Dr. Morin that more than one methodology should be used to estimate a cost of equity: "None of them are constantly reliable. So you have to rely on more than one methodology in order to make sure you're getting an accurate estimate of what the current cost of equity is." Tr. p. 1999, l. 11-14.

electricity demand between 2007 and 2030 as projected by the Federal Energy Information Administration,[22] plus inflation projected by the Congressional Budget Office for the period 2016-2019[23] as the growth rate for the third stage of his DCF analysis (years 11 through infinity),[24] which also significantly impacted the growth rate in the second stage of his analysis (years 6 through 10). Mr. Murray apparently invented the idea of using projected electricity demand growth adjusted for inflation in this way, and his unconventional calculation produced a very low growth rate of about 3.1%.[25] It is unclear why Mr. Murray thought a measure of inflation, which is typically tied to dollar amounts, would also be an appropriate method of escalating kilowatts of demand for electricity.

Staff argues that Mr. Murray's Stage 3 growth rate will "more accurately model normal growth, consistent with industry fundamentals."[26] However, the testimony of other experts shows that Mr. Murray's use of this growth rate is simply wrong. Dr. Morin testified that this growth rate "is based on demand growth and not on earnings/dividends growth as *required* by the DCF model."[27] In other words, the model requires an input of the projected *dollar* growth in earnings and/or dividends, not the projected growth in kilowatts of electricity demand. Mr. Lawton, OPC's witness, explained at the hearing why the dollar growth in earnings/dividends might greatly exceed the growth in electricity demand through, for example, the development of new services, and why therefore use of the projected growth in electricity demand as a growth measure in the DCF is incorrect. Mr. Lawton also noted that projections of growth in electricity

[22] Ex. 200, p. 26, l. 15-20 (Staff Report).
[23] *Id.* p. 26, l. 24-26.
[24] There is an obvious timing mismatch among Mr. Murray's third stage (years 11 through infinity), the period he used for growth in electricity demand (2007-2030) and the years he used for his inflation estimate (2016-2019).
[25] Ex. 200, p. 27, l. 7-8.
[26] Staff's Initial Brief, p. 28.
[27] Ex. 112, p. 18, l. 1-2 (Morin rebuttal) (emphasis original).

demand vary considerably and therefore any particular growth rate selected may be incorrect. In response to questions from Staff counsel, Mr. Lawton testified as follows:

Q. I believe that your testimony has indicated that as shown on the—the schedule attached to Mr. Hill's testimony, that average EPS growth as shown on that chart for the last 50-odd years is about 3.3 percent, correct?

A. *That is correct.*

Q. And as shown on the chart or graph attached to the rebuttal testimony of Mr. Murray, this chart shows—chart—chart shows that electric demand growth is approximated to be roughly 1 percent from, let's say, 2012 through 2035. Will you accept that?

A. *That's what it shows.*

Q. Okay. Given that information, can you help me explain how—can you help me understand how investors will accept the proposition that EPS will grow at 5-plus percent into perpetuity?

A. *That's not a yes-or-no answer.*

Q. That's not a yes-or-no answer.

A. *Okay. Number one, the—the predicate to your question assumes that this growth rate forecast is, in fact, correct. And I think if you look around the country, you'll find very different forecasts for growth in energy as well as demand for utilities.*

Second, you've got to look at utilities and where their funds come from. They not only come from the changes in electricity, but additional services are being provided by many utilities across the country. We've heard talk about smart meters and different services, and it's not all reliant totally upon the growth in electricity.

If you do by analogy or look by analogy to the telephone industry and what we have with the cell phones and all the other services provided by telephone companies and the additional revenues provided by telephone companies, you'll see that maybe service for telephones hasn't exploded, but certainly the various services in additional ways of earning revenues have increased and changed over times.

> *So with that, I—I—the current forecasts are 5 percent, that's what the analysts are estimating. That's what investors are going to be looking at. It's available to investors and I think you can rely upon it.*[28]

Mr. Murray's use of projected electric demand growth adjusted for inflation as his Stage 3 growth rate is beyond bad judgment, it is simply wrong. Because this analysis is the foundation for his recommended range and midpoint, those too must be rejected.

The Staff's Initial Brief also attempts to defend Mr. Murray's use of earnings projections contained in equity analysts' reports and projected earnings of MOSERS to test the reasonableness of his recommendations. The Staff argues that "these references demonstrate that Staff's recommendation is consistent with the expected returns used by those in the investment community."[29] In its initial brief, AmerenUE referenced the testimony of AmerenUE witness Julie Cannell, a former equity analyst who is thoroughly familiar with the type of reports Mr. Murray is using, to explain why these reports are inappropriate for use in determining an appropriate ROE for AmerenUE. Specifically, Ms. Cannell explained why the projected earnings of a particular company at a particular time could be far higher or lower than the cost of equity for that company. For example, in Ameren Corporation's case, Goldman Sachs (whose report is one of the reports Mr. Murray relies upon) has a "sell with conviction" recommendation for the company. It is quite obvious that Goldman Sachs' projection of the company's actual earnings is *below* what it believes the cost of equity capital is given that at its projection it recommends investors sell, and sell "with conviction," the company's stock. Consequently, its projection of actual earnings has no relevance at all to AmerenUE's cost of equity.[30]

Mr. Lawton also testified that he is concerned about using equity analysts' reports in the way Mr. Murray has, and there are problems with such use of equity analyst reports because they

[28] Tr. p. 2182, l. 19 to p. 2184, l. 14.
[29] Staff's Initial Brief, p. 36.
[30] Equity analysts' projections of earnings below 9% obviously do not reflect a defensible cost of equity for electric utilities.

are not generally available to average investors.[31] Dr. Morin also weighed in on Mr. Murray's unconventional and misguided use of equity analysts' reports. Dr. Morin testified that:

> [r]eliance on selected equity research reports to support Mr. Murray's recommendation does not provide the kind of analysis that would allow this Commission to make a reasonable determination of the appropriate ROE. A handful of equity reports is a highly questionable source of information in assessing an appropriate ROE for a regulated utility and in gauging the academic state of the art in the field of finance.[32]

Dr. Morin was even more critical of Mr. Murray's reliance on actuarial data used for pension fund accounting by MOSERS. Dr. Morin testified that this information is "irrelevant in estimating a utility's cost of capital." [33] Dr. Morin testified:

> This comparison, in the context of a rate proceeding, is highly unusual and inappropriate. To the best of my knowledge, I only know of one cost of capital witness (Mr. Stephen Hill, who was the Staff's ROE witness in the Company's last rate case) comparing an individual utility's ROE to a pension fund's actuarial data in all the years that I have provided rate of return testimony. Additionally, I am unaware of any regulatory commission that has relied on such data. Indeed, the California Public Utilities Commission recently considered similar arguments from Mr. Hill and concluded as follows:
>
> *The objectives of a pension fund are fundamentally different from that of an equity investor in a single utility and the risk profiles are not comparable. The Employee Retirement Income Security Act dictates that pension funds must be diversified whereas a utility's ROE is based on risks specific to that utility's operations.*
>
> *More importantly, pension fund returns are related to market value of assets held in the pension fund while a utility's ROE is applied to a book value rate base…Pension fund assumptions are not comparable to the ROE used in utility ratemaking. Having resolved this issue, PG&E [the utility] should not be required to continue comparing its pension return assumptions to its ratemaking ROE in future ROE proceedings. In re S. Cal. Edison Co., 262 P.U.R. 4th 53, 72 (Ca. Pub. Utils. Comm'n 2007).*[34]

Dr. Morin further testified that he agreed with the reasoning of the California Public Utilities Commission. He stated that "[a]ctuarial data utilized for pension fund accounting are by nature very

[31] Tr. p. 2212, l. 20 to p. 2213, l. 22.
[32] Ex. 112, p. 27, l. 21 to p. 28, l. 3.
[33] Ex. 112, p. 25, l. 11-12.
[34] Ex.112, p. 26, l. 1-30.

conservative, consistent with Generally Accepted Accounting Principles, and are not well suited for assessing the cost of equity capital in a rate proceeding. By virtue of the very long-term nature of pension fund assets, projected returns on pension fund assets are not indicative of the cost of equity in the context of a regulatory proceeding. Moreover, the actuarial data on which Mr. Murray relies—namely just one particular corporate actuary's assumptions (MOSER) is very selective." [35]

Mr. Lawton also agreed that the use of retirement plan information is unusual and problematic due to the differences in portfolio goals. Mr. Lawton testified as follows:

> Q. Okay. Mr. Murray also relied on the Missouri State Retirement System, some information to confirm the results of his analysis; isn't that correct?
>
> A. *That's correct.*
>
> Q. Do you recall ever seeing anybody but Mr. Murray rely on this kind of information in estimating a cost of equity?
>
> A. *Generally, no. I think I pointed out in deposition I saw Mr. Murray rely upon it in a—in a prior case I testified in Missouri.*
>
> Q. Okay. But nobody other than Mr. Murray?
>
> A. *That is correct.*
>
> Q. Okay. And isn't it true that retirement plans generally have different portfolio goals than electric utility stocks?
>
> A. *Oh, they may have electric utility stocks in their portfolio. I think it's based on different portfolio goals than the average investor. And—and—and if I'm investing for my retirement and I'm—that may be different portfolio than if I'm a young man and I'm trying to see some real growth and—and—and make some money in the market and—*
>
> Q. And that—so that—
>
> A. *--may have different goals.*
>
> Q. Is that the problem with using retirement system data in this way?

[35] Ex. 112, p. 26, l. 33 to p. 27, l. 5.

A. *Yes.*[36]

Staff did not bother to defend Mr. Murray's use of his inexact "rule of thumb" in its initial brief, so there is nothing to respond to with regard to that "test of reasonableness." The bottom line is that Mr. Murray has chosen unconventional and inappropriate measures in his attempts to justify the extremely low ROE he developed by incorrectly calculating his multi-stage DCF. These measures are not relied upon by other experts or commissions, and they should not be relied upon in this case.

Staff's Initial Brief also defends Mr. Murray's calculation of the more traditional constant-growth DCF, which produced a range of 9.2%-10.2%.[37] Although Mr. Murray calculated this DCF result, he did not use it to develop his range or midpoint recommendation. The traditional constant-growth DCF model is one of the best models to use in estimating an ROE for a public utility. However, Mr. Murray has again tainted his results by using an inappropriately low growth rate. Staff's Initial Brief says that Mr. Murray's growth rate of 4%-5% was "based upon Staff's expert judgment," but in fact these growth rates are based on no data and appear to have been pulled out of thin air by Mr. Murray:

Q. And my understanding is for the growth component of the constant growth DCF analyses, you used 4 to 5 percent; is that correct?

A. *Yes.*

Q. And I think you—in your deposition, you referred to that as a very generic growth rate that you had just thrown in; is that correct?

A. *Yes.*

Q. Okay.

A. *It's generic and it's based on Staff's experience of what—what type of electric utility growth rates we've used in constant growth DCFs in the*

[36] Tr. p. 2211, l. 16 to p. 2212, l. 19.
[37] Staff's Initial Brief, p. 21.

past where we felt like those growth rates were much more sustainable, at least myself I should say.

Q. And would it be fair to say that your 4 to 5 percent growth rate is based on your judgment:

A. *Yes, it is.*

Q. It's not like there's a quantifiable schedule like there is for the dividend component of the—

A. *There's no mechanical calculation to it, no.*[38]

Mr. Murray's selection of a generic growth rate based exclusively on his "judgment" stands in stark contrast to the other experts, who based their growth parameters for the constant-growth DCF on published, projected earnings estimates.[39] Staff has also used this approach in prior cases.[40] Mr. Murray testified that if he had used projected growth rates in his constant-growth DCF analysis, the results would have been 11.22%:

Q. Well, if you had used projected growth rates for your constant growth DCF analysis in this case, isn't it true that you would have used 6.02 percent instead of 4 to 5 percent?

A. *Yes.*

Q. Okay. And then if you would have done that, you would have added the 6.02percent to your 5.2 percent [Mr. Murray's dividend yield component of the formula] and get a result of 11.22 percent; is that correct?

A. *Yes.*[41]

Since projected earnings estimates are clearly appropriate for use as the growth parameter in the constant-growth DCF formula, Mr. Murray's evidence supports a constant-growth DCF result of 11.22%.

[38] Tr. p. 2037, l. 14 to p. 2038, l. 10.
[39] Ex. 408, p. 23, l. 1-6 (Gorman direct); Ex. 304, p. 23, l. 10-23 (Lawton direct); Ex. 111, p. 42, l. 14 to p. 43, l. 13 (Morin direct); Ex. 112, p. 53, l. 15-19.
[40] Tr. p. 2038, l. 11-21.
[41] Tr. p. 2040, l. 1-10.

B. MIEC's Initial Brief does not provide justification for MIEC witness Gorman's unreasonably low ROE recommendation.

As AmerenUE explained in its initial brief, MIEC witness Michael Gorman has recommended a range and midpoint ROE that are clearly too low.[42] The primary reasons that Mr. Gorman's recommended ROE is too low are:

- Mr. Gorman's recommendation is too heavily influenced by his very low CAPM result of 9.54%. This result forms the bottom end of Mr. Gorman's range and is weighted 50% in the calculation of Mr. Gorman's midpoint. As detailed in AmerenUE's Initial Brief, several of the witnesses to this proceeding have testified about problems with the CAPM method, and those problems have caused it to produce unreasonably low results in this case.

- Aside from the generic problems with Mr. Gorman's over-reliance on the relatively unreliable CAPM method, the evidence shows that Mr. Gorman's particular CAPM result is unreasonably low for two reasons. First, Mr. Gorman did not temper his "plain vanilla" CAPM result by conducting an Empirical CAPM analysis as both Dr. Morin and Mr. Lawton did. As Dr. Morin testified, the ECAPM adjusts for the fact that the "plain vanilla" CAPM underestimates ROEs for lower beta (i.e. lower risk) enterprises such as electric utilities, and produces a higher ROE. Mr. Lawton agreed, and testified that he did not dispute that the ECAPM is an appropriate adjustment.[43] Second, the evidence shows that Mr. Gorman used a market risk premium component of his CAPM analysis which was too low. Mr. Gorman used an average of a 5.7% and a 6.5% market risk premium to develop his CAPM result of 9.54%. However, he testified: "I will not take issue with the market risk premium of 6.5% used by Dr. Morin, because it appears to be in line with a normalized risk premium."[44] If Mr. Gorman had simply used a 6.5% market risk premium, this adjustment alone would have increased his CAPM result to 9.84%, and his midpoint ROE to 10.15%.[45]

- Mr. Gorman has "watered down" the impact of his traditional constant-growth DCF result by averaging it with two other DCF analyses—the

[42] As AmerenUE noted, the very top of Mr. Gorman's recommended range, 10.5%, which Mr. Gorman agreed would be reasonable for the Commission to adopt (Tr. p. 1959, l. 1-4), would be close to a reasonable ROE as measured by the 10.59% national average and Dr. Morin's 10.8% recommendation.
[43] Ex. 112, p. 24, l. 10 to p. 25, l. 8; Tr. p. 2203, l. 22 to p. 2204, l. 3; Tr. p. 2204, l. 13-15.
[44] Ex. 409, p. 5, l. 18-20 (Gorman rebuttal).
[45] The adjusted CAPM is calculated by averaging the CAPMs for the two proxy groups in the "High" column on Schedule MPG-19 (which reflects a 6.5% market risk premium). Specifically 9.72% (line 4) + 9.96% (line 9) = 19.68 divided by 2 = 9.84%. The adjusted midpoint it equal to Mr. Gorman's average DCF result (10.46%) plus the adjusted CAPM (9.84%) divided by 2 = 10.15%.

multi-stage growth DCF, which the Commission has used in recent cases, and the constant growth-sustainable growth method, which this Commission has never used to establish an ROE. If Mr. Gorman's DCF analyses had been considered separately, his range and midpoint would have been much higher.

- Mr. Gorman has arbitrarily changed his DCF analyses in several ways from his analyses in AmerenUE's last rate case, which have the effect of materially lowering the results. Specifically, he has switched to using the *median* growth results for the proxy groups rather than the *average* results. Also, he completely excluded the growth results for one of the two proxy groups when calculating his sustainable growth DCF.

Adjusting Mr. Gorman's analysis to fix some or all of these problems will move Mr. Gorman's midpoint to somewhere at or near the national average ROE.

In its initial brief, MIEC states that "…the average ROE awards of other regulatory agencies should not be considered competent and substantial evidence of the ROE required by AmerenUE's investors."[46] It is understandable that MIEC would not want this information considered by the Commission, particularly since Mr. Gorman is recommending an ROE for AmerenUE that is a full 59 basis points below the national average for integrated electric utilities and 20 basis points below the lowest ROE authorized for any integrated electric utility in 2009.[47] However, notwithstanding MIEC's resistance to consideration of this information, under *Bluefield* and *Hope* it must be considered. As the Commission has stated: "Cost of capital can be defined as the return investors expect to receive on alternative investments of comparable risk." Remember that the United States Supreme Court in the *Bluefield* case said a public utility is entitled to rates that will permit it to earn a return equal to the return being earned on

[46] MIEC's Initial Brief, p. 38.

[47] It is important to point out that the relevant statistic is the average authorized ROE for ***integrated*** electric utilities, which in 2009 was 10.59% based on Regulatory Research Associates (now SNL) data. Ex. 112, p. 6, l. 25-28. Staff's Initial Brief improperly cites a 10.47% average ROE for all electric utilities for the first 9 months of 2009. Dr. Morin and Mr. Lawton have acknowledged, and the Commission has previously found, that wires only utilities are generally less risky, and therefore have a lower return than integrated electric utilities like AmerenUE. Ex. 112, p. 7, l. 6-8; Lawton: Tr. p. 2188, l. 9-24; *Re: Union Electric Company d/b/a AmerenUE*, Case No. ER-2008-0318, *Report and Order* (January 27, 2009), p. 18: "That overall average number includes all electric utilities, some of which are 'wires only' utilities in restructured states that provide only distribution services and do not own generation assets. Such utilities tend to be less risky and generally receive lower authorized returns on equity."

investments in businesses with corresponding risks and uncertainties. [citation omitted.]" In affirming the Commission's decision in AmerenUE's last rate case, Case No. ER-2007-0002, the Missouri Court of Appeals recognized the relevance of considering the national average of authorized ROEs in determining an authorized ROE for a Missouri utility:

> The United States Supreme Court has instructed the judiciary not to interfere when the commission's rate is within the zone of reasonableness. *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 767, 88 S.Ct. 1344, 20 L.Ed.2d 312 (1968) ("courts are without authority to set aside any rate selected by the Commission [that] is within a 'zone of reasonableness'). Moreover, the commission found that UE was seeking to raise capital across the entire nation, which supported the commission's using the national average.[48]

Consequently, MIEC's statement that the "the average ROE awards of other regulatory agencies should not be considered" is simply wrong and directly contradicts the legal standards that bind this Commission.[49]

MIEC's reluctance to have this information considered is perhaps due to the fact that they like to focus on a different standard contained in the *Bluefield, Hope, and Permian Basin* decisions—the standard that requires the Commission to authorize a return sufficient to insure the financial integrity of the utility, which MIEC acknowledges is "an appropriate concern for this Commission."[50] MIEC makes a special point to say that if Mr. Gorman's ROE is adopted, that decision will not result in a downgrade of AmerenUE's current "BBB" investment grade bond rating. (*Id.*) Unfortunately for MIEC, the law requires more. In particular, the law also requires the Commission to authorize a return equal to the return being earned on investments having corresponding risks and uncertainties, which makes the authorized ROEs for businesses that are the most similar to AmerenUE—other integrated electric utilities—relevant to determination of an appropriate ROE for AmerenUE. The Commission should continue its

[48] *State ex rel. Office of the Public Counsel*, 274 S.W.3d 569, 574 (Mo. App. W.D. 2009).
[49] Both Dr. Morin and Mr. Lawton have also testified that it is relevant for the Commission to consider the ROEs authorized by other Commissions in reaching its decision (Ex. 112, p. 6, l. 20-28; Lawton: Tr. p. 2214, l. 10-21).
[50] MIEC Initial Brief, p. 48.

practice of considering this information whenever it sets an authorized ROE for an electric utility.

There are other important points of reference that MIEC's Initial Brief ignores. For example, this Commission very recently authorized a 10% ROE for Missouri Gas Energy, a gas distribution utility with a risk profile that is much less risky than AmerenUE's.[51] For one thing, MGE is a distribution company, so it has none of the substantial risks AmerenUE faces in operating large generating facilities, including a nuclear plant and four baseload coal units. In addition, MGE's distribution operation arguably faces less risk; underground gas pipelines are not subject to weather-related outages like an electric distribution system. MGE also has a PGA mechanism that consistently provides it full recovery of its gas costs. This is in contrast with AmerenUE's FAC which provides only 95% recovery of changes in net fuel costs. And finally, and perhaps most significantly, MGE was permitted to use straight-fixed-variable rate design, which permits it to recover all of its costs through fixed charges. This eliminates almost all financial risk for the Company, and as Mr. Lawton testified, provides a virtual guarantee of cost recovery absent customers leaving the system.[52] AmerenUE's much different risk profile suggests that an authorized ROE materially higher than MGE's—in the neighborhood of the national average for electric utilities and Dr. Morin's recommendation of 10.8%[53]–is warranted.

As a final point of reference relevant to Mr. Gorman's recommendation, it is noteworthy that Mr. Gorman is recommending an ROE of 10% for Ameren's Illinois electric distribution operations in cases that are currently pending before the Illinois Commerce Commission.[54]

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[51] *Re: Missouri Gas Energy*, File No. GR-2009-0355, *Report and Order* (February 10, 2010).
[52] Tr. p. 2189, l. 19-23.
[53] MIEC's Initial Brief contains a chart that erroneously suggests that Dr. Morin is recommending a range of ROEs. MIEC Initial Brief p. 40. In fact, Dr. Morin does not recommend a range, but only recommends a 10.8% return on equity. Ex. 112, p. 55, l. 16-17.
[54] Tr. p. 1981, l. 13-15.

Again, since AmerenUE is an integrated electric utility with generation related risk, it seems that Mr. Gorman should be recommending a higher ROE.

For all these reasons Mr. Gorman's recommendation should be adjusted significantly upward, if it is considered at all by the Commission.

C. OPC's Initial Brief fails to justify Mr. Lawton's unreasonably low midpoint ROE recommendation.

OPC witness Lawton recommends a range of ROEs that runs higher than Dr. Morin's recommendation—to 10.9%—and he has testified that adoption by the Commission of any ROE within his range would be reasonable. So in some respects, AmerenUE has no reason to object to Mr. Lawton's recommendation. However, Mr. Lawton's midpoint of 10.1%, like Mr. Gorman's 10.0% recommendation, is overly influenced by risk premium analyses (CAPM and risk premium) which form the bottom boundary of his range and exert 50% influence on his midpoint.[55] Moreover, like Mr. Gorman's recommendation, Mr. Lawton's midpoint does not compare favorably to the points of reference cited earlier in this brief—the national average ROE, the lowest ROE authorized for any integrated electric utility in 2009, and the MGE decision. OPC's Initial Brief does not address any of these issues, or provide any compelling justification for using Mr. Lawton's midpoint without adjusting to account for these factors.

OPC's Initial Brief does suggest that AmerenUE's alleged "equity rich updated capital structure" indicates that the ROE authorized for the company should be lower than it otherwise would be.[56] However, the evidence shows that AmerenUE's capital structure is actually less "equity rich" than it was last rate case. In this case, the Company's actual capital structure has an equity ratio of 51.26%, whereas last rate case, the Commission-approved capital structure for

[55] As explained in detail in AmerenUE's Initial Brief, Mr. Lawton has expressed concerns about the use of these methods. AmerenUE's Initial Brief, pp. 31-32.
[56] OPC's Initial Brief, p. 14.

AmerenUE was 52.009% equity.[57] No one claims that these equity ratios are not within the normal range of equity ratios for an electric utility. No party proposed any type of adjustment in either case, and an adjustment to the ROE on this account is not warranted or supported by any evidence in this case.

One final point in OPC's Initial Brief needs to be addressed. OPC states that it "…does not believe that the Commission should recalculate every witness' ROE recommendation as AmerenUE attempted to do in cross-examination of witnesses Lawton and Gorman." This contention, like MIEC's contention that the national average should not be considered, is contradicted by applicable case law. OPC raised essentially this same argument in the appeal of Case No. ER-2007-0002, where Mr. Gorman had recommended an ROE of 9.8%, but where the Commission had expressed concerns with *how* Mr. Gorman arrived at that number, made adjustments to Mr. Gorman's calculations, and authorized an ROE of 10.2%. The Court of Appeals confirmed that the Commission is free to determine the appropriate ROE and is not obligated to blindly adopt the recommendation of any one witness. The court stated:

> The commission was not obligated to believe all of Gorman's testimony.... [58]

As this case demonstrates, taking into account adjustments a witness should have made is precisely what the Commission must do to fulfill its duty to set just and reasonable rates in this case. The Commission must recognize that all of the witnesses are sponsored by parties that have a vested interest in the outcome of this rate case.[59] The Commission should not, and is not required to, accept any witness' analysis at face value. It should consider the details of the analysis each witness presents, measure the results against appropriate benchmarks (e.g., average

[57]Ex. 180, Schedule GSW-TE29-3; *Re: Union Electric Company d/b/a AmerenUE*, Case No. ER-2008-0318, *Report and Order* (January 27, 2009), p. 15.
[58] ***S****tate ex rel. Office of the Public Counsel*, 274 S.W.3d at 575.
[59] Staff, the one party that ought to be neutral, has demonstrated its lack of neutrality throughout this case, most especially with regard to the ROE and depreciation issues.

ROEs authorized for other integrated electric utilities, previous Missouri Commission decisions) and make its own decision about the appropriate ROE.

D. An adjustment to reflect the quarterly payment of dividends is appropriate.

As part of his recommendation, Dr. Morin included a 20 basis point adjustment to his DCF analyses to account for the fact that dividends are paid on a quarterly, rather than on an annual basis.[60] Such an adjustment has been approved by the Commission in all recent decisions regarding ROE, including AmerenUE's last rate case.[61] Staff and OPC both oppose this adjustment, and argue in their initial briefs that the Commission should change its practice of including such an adjustment in its calculation of ROEs.[62]

In AmerenUE's last rate case, the Report and Order addressed this issue as follows:

> One more adjustment to Gorman's recommended return on equity is appropriate. Gorman used an annualized quarterly dividend payment in calculating his DCF analyses. AmerenUE as well as the overwhelming majority of traditional vertically-integrated electric utilities pay dividends quarterly, not annually. This distinction is important because the conventional DCF model does not account for the compounding of interest (earnings) investors receive and expect in the real world. So, it is more appropriate to use a quarterly DCF model.
>
> At the hearing, Dr. Morin further explained that the use of the annual DCF model is appropriate in jurisdictions that use a forward test year to avoid being overly generous to the company. However, in a jurisdiction such as Missouri that uses a historical test year, the quarterly test year is more appropriate. Morin indicated the difference between the quarterly and the annual DCF model would "definitely" add 20 basis points to a return on equity recommendation. However, Morin's analysis does not contemplate the greater amount of equity in AmerenUE's capital structure referenced by the Commission earlier. Therefore, the Commission finds that only a five basis point adder is appropriate in this case.[63]

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[60] Ex. 112, p. 54, l. 25 to p. 55, l. 17.
[61] *See, for example Re: The Empire District Electric Company,* Case No. ER-2008-0093, *Report and Order* (July 30, 2008), p. 21.
[62] Staff's Initial Brief, pp. 24-26; MIEC's Initial Brief, pp. 41-43.
[63] *Re: Union Electric Company d/b/a AmerenUE*, Case No. ER-2008-0318, *Report and Order* (January 27, 2010), pp. 23-24.

The evidence in this case clearly supports continuation of the adjustment to account for quarterly dividend payments. In criticizing Mr. Murray for failing to include such an adjustment, Dr. Morin testified:

> The two annual DCF models used by Mr. Murray ignore the time value of quarterly dividend payments and assume that dividends are paid once a year at the end of the year. Since investors are aware of the quarterly timing of dividend payments, this knowledge is reflected in stock prices. As I show in Chapter 11 of my book, *The New Regulatory Finance*, the use of the annual version of the DCF model understates the cost of equity by approximately 20 basis points, depending on the magnitude of the dividend yield component.
>
> By analogy, a bank rate on deposits that does not take into consideration of the interest payments understates the true yield if you receive the interest payments more than once a year. The actual yield will exceed the nominal interest rate.[64]

Effectively the annual DCF model assumes that utilities hold dividends until the end of the year, when actually the utility loses the time value of the money by paying the dividends out quarterly.

Dr. Morin also provided testimony in response to Mr. Gorman's failure to include a quarterly dividend adjustment.

> Mr. Gorman argues that the return from the reinvestment of dividends is not a cost to the utility and, therefore, should not be included in the allowed ROE. I disagree…Since the stock price employed in the DCF model to determine investor returns reflects a quarterly stream of dividends, it stands to reason that the quarterly nature of dividend payments be explicitly recognized. Cash flows, that is, dividends, are actually received quarterly. Thus a quarterly model should be applied….Moreover, by paying the dividends earlier (at the end of the first, second and third quarters, and not all at once at the end of the year), the utility is deprived of the cash that it pays earlier, which indeed does have a cost to the utility.[65]

Dr. Morin's adjustment simply accounts for that opportunity cost to the utility, which obviously occurs whenever dividends are paid quarterly. Staff witness Stephen Hill had to acknowledge that opportunity costs are attendant to the quarterly payment of dividends. Mr. Hill testified as follows:

[64] Ex. 112, p. 19, l. 14-23.
[65] *Id.* p. 47, l. 9-21.

Q. You had a fairly long discussion with Commissioner Davis about quarterly dividends and how that should be handled in the cost of equity in a rate case, right? Do you remember that?

A. *Yes.*

Q. If the company pays $200 million of dividends annually but pays $50 million on March 31st, $50 million on June 30th, 50 million on September 30th and 50 million on December 31st, isn't it true that there's an opportunity cost to the utility company itself of not having use of the first $50 million payment that it made from April 1 to 12/31? Isn't there an opportunity cost associated with that?

A. *Yes.*

Q. And there's an opportunity cost associated with the next 50 million between July 1 and 12/31, isn't there?

A. *Yes. That's always been the case with utilities that pay quarterly.*

Q. And that opportunity cost is equal to the utility's weighted average cost of capital during the subject period, isn't it?

A. *You could calculate it that way.*[66]

The parties arguing against application of the Commission's normal quarterly dividend adjustment simply don't want to recognize that this opportunity cost exists for utilities paying quarterly dividends, as compared to the DCF model that assumes dividends are paid at the end of the year. These parties have provided no evidence that would justify the Commission's departure from its practice of making a quarterly dividend adjustment to the calculation of AmerenUE's ROE, and their unsupported arguments in this regard should be rejected.

E. Staff's use of geometric averages rather than arithmetic averages in calculating the market risk premium component of the CAPM is incorrect.

In its initial brief, Staff argues that it is more appropriate to use geometric averages than arithmetic averages in calculating the market risk premium component of the CAPM.[67]

[66] Tr. p. 2127, l. 22 to p. 2128, l. 19.
[67] Staff's Initial Brief, pp. 33-34.

However, Dr. Morin testified that Mr. Murray's reliance on geometric means in calculating his CAPM is inappropriate. He testified:

> Only arithmetic means are appropriate for forecasting and estimating the cost of capital, and geometric means are not. Indeed, then Morningstar publication from which Mr. Murray derives his MRP estimate contains a detailed and rigorous discussion of the impropriety of using geometric averages in estimating the cost of capital. There is no theoretical or empirical justification for the use of geometric mean rates of returns when estimating the cost of capital.[68]

Dr. Morin further testified that Mr. Murray's use of the geometric mean market risk premium of 3.9% rather than the arithmetic mean of 5.6% significantly understates the market risk premium, and suggests an understatement of his CAPM results by 112 basis points.[69]

In response to questions from Commissioner Davis, Dr. Morin amplified his discussion of the advantages of arithmetic vs. geometric means:

> Q. Right. Okay. Now let's go to CAPM analysis. You, Mr. Gorman and Mr. Lawton, I believe, all use an arithmetic mean; is that correct?
>
> A. *Yes, sir, that's correct.*
>
> Q. Did Lawton do a geometric mean, too?
>
> A. *I think he gives weight to the arithmetic mean, and that's the right way to do it.*
>
> Q. And why is that?
>
> A. *Well, the technical reason is that the CAPM is an additive model, so the expected rate of return is an arithmetic mean of one period. If you kind of visualize in your mind a bell-shaped distribution of returns the investor's looking at, the arithmetic mean is the central tendency, the expectation, the middle of that bell-shaped curve. That's the technical reason.*
>
> *The second reason is, that geometric mean is a very good measure of performance of a portfolio over a long historical period, but the problem is it doesn't tell you anything about the trip on the way from year one to year ten, for example. You can have a stock that's very, very, very volatile and one that's very, very, stable and they both have the same geometric*

[68] Ex. 112, p. 23, l. 7-15
[69] *Id.* p. 23, l. 17-19.

mean, but the investor would require much higher rate of return on the volatile stock than the one that's very, very steady, and the geometric mean doesn't pick that up. The arithmetic mean incorporates volatility, if you wish.

So those are the two main reasons, to keep it, you know, nontechnical, why one would prefer an arithmetic mean. The Ibbotson Yearbook, of course, where we all get our data, strongly advocates the use of the arithmetic mean, and most of the leading textbooks in finance also advocate the arithmetic mean for measuring the cost of equity.

That doesn't mean we can't use a geometric mean for some other purpose like figuring out performance of a mutual fund over the last 20 years. There's nothing wrong with that.[70]

Based on Dr. Morin's testimony, the Commission should not adopt the use of geometric means for purposes of CAPM analyses as Mr. Murray suggests.

II. DEPRECIATION.

Perhaps the most striking feature of the depreciation discussion in the Staff's Initial Brief is that it bears so little resemblance to the arguments the Staff made through three rounds of pre-filed testimony. Moreover, it contains a number of statements, represented as though they are based in fact and in the record, but for which there is no support in the record.

Among the undisputed facts that *are* supported by the record that rebut virtually every point the Staff now makes are the following:

- All authoritative sources and the Staff's own depreciation manual agree that the four steam production plants are life span property, and the NARUC depreciation manual specifically states that power plants are "most appropriately" studied using the life span method and that indeed life span property *requires* a different analysis than mass property;[71]
- The underlying premise of the Staff's treatment of these power plants as mass property fails:
    - There is, as the Staff admits, insufficient retirement history to provide a "true [reliable] mass property" result;

[70] Tr. p. 1882, l. 9 to p. 1883, l. 20.
[71] AmerenUE's Initial Brief, pp. 45 - 46, in particular the discussion in connection with fns. 96 – 102.

- A statistically significant analysis could not be done; and
- In Staff witness Arthur Rice's words, it is "probably correct" that an un-depreciated balance will be left (for future ratepayers not served by the plants) when these plants retire, which means the Staff's unusual treatment does not recover the service value of these plants over their service lives.[72]

- Mr. Rice admits that if there is inadequate retirement history you "really *can't* use the mass property approach"[73] (emphasis added), yet he did so anyway;
- Virtually all jurisdictions use the life span approach for steam production plants;[74]
- AmerenUE witnesses John Wiedmayer and Larry Loos, as well as MIEC witness James Selecky, all use the life span approach,[75] save Mr. Selecky's one-time opportunistic use of the mass property approach in this case alone (using depreciation parameters the Staff agrees are flawed and unreliable);
- The estimated life spans developed by Black & Veatch – from 61 to 72 years – are longer than Mr. Selecky typically sees,[76] and exceed the 55-year average life span being used across the country by other commissions to depreciate steam production plants;[77]
- The Staff incorrectly represented to the Commission that the Commission "rejected" the life span approach;[78]
- The Staff incorrectly represented to the Commission that it was following "Commission policy";[79]
- The Staff's treatment of the four steam plants is inconsistent with its treatment of the Callaway Plant, a fact lead Staff auditor Stephen Rackers recognized;[80]

[72] AmerenUE's Initial Brief, pp. 49-51, in particular the discussion in connection with fns. 110-116.
[73] Ex. 108, p. 9, l. 8 to 22 (Loos surrebuttal) (quoting Rice Deposition, p. 74, l. 18-23).
[74] Ex. 104, p. 30, l. 7-10 (Wiedmayer direct).
[75] AmerenUE's Initial Brief, p. 46.
[76] Tr. p. 1482, l. 14-21.
[77] Ex. 107, Sch. LWL-E1, Appx. A-1 (Loos direct).
[78] Ex. 216, p. 1, l. 23-24 (Rice rebuttal).
[79] Ex. 200, p. 97, l. 19; Ex. 217, p. 10, l. 13 (Rice surrebuttal).
[80] Ex. 167 (E-mails from Steve Rackers).

- Mr. Rice himself agrees that these four steam plants are likely "going away" in the next 12 to 36 years – which coincides exactly with the estimated retirement dates used by the Company in this case;[81] and

- Mr. Rice agrees the Black & Veatch study was "well done," "rational," "relatively complete, logical," and is "as reliable, or at least within a reasonable range of reliability, of what could be done today."[82]

A. The Staff's Brief is replete with unsupported conclusions or conclusions that are contradicted by the record itself.

"Proper recovery depends on the quality of the information used, not the choice of method."[83] To the extent that statement is true, it proves the Company's case.[84] The quality of the information used by the Staff is poor, as the Staff admits and as the discussion of the record in this case at pages 49 to 54 of the Company's Initial Brief demonstrates. By contrast, the quality of the life span analysis in this case is high, as the Staff also admits and as the discussion of the record in this case at pages 56 to 57 and 62 to 63 of the Company's Initial Brief also demonstrates.

Staff's contention in its brief that "it is not possible to calculate reliable estimates" of the retirement dates of these plants is completely refuted by the record.[85] Had Mr. Rice's supervisor, Guy Gilbert, let Mr. Rice use the life span approach, Mr. Rice "would have done something very similar to what Mr. Loos did"[86] – i.e., the Black & Veatch plant life study. When Mr. Selecky uses the life span approach (which he always does, save this case), he essentially does an analysis very similar to the Black & Veatch analysis.[87] Mr. Selecky also had no material

[81] Ex. 168 (E-mail from Rice to Gilbert).
[82] AmerenUE's Initial Brief, pp. 62-63, in particular Mr. Rice's admissions as noted in connection with fns. 146-151.
[83] Staff's Initial Brief, p. 44.
[84] In fact, as the record in this case shows, the mass property approach shouldn't be used for life span property at all, but in any event, it certainly shouldn't be used (and as Mr. Rice conceded, can't be used) when the data is insufficient, as here.
[85] Staff's Initial Brief, p. 44.
[86] Tr. p. 1400, l. 15-18.
[87] Tr. p. 1483, l. 10-23.

criticism of the Black & Veatch study, save his argument that the Meramec Plant's retirement date should be moved out by five years.[88]

Staff's criticism of the lack of an "economic analysis" (*see, e.g.*, Staff's Initial Brief, p. 45) underlying the estimated retirement dates, the earliest of which is still 12 years into the future, is a red herring as well. Mr. Rice admits than an economic analysis *cannot be done*.[89] Mr. Loos testified that the advantage of such an economic analysis would be very minimal, and that in any event he would not conduct such an analysis without the benefit of the analyses he did conduct.[90] Somehow other state commissions and their staffs and Messrs. Wiedmayer, Loos and Selecky, as well as the NARUC depreciation manual and the Wolf and Fitch text on depreciation, are all able to endorse development of reasonable (not certain, but reasonable) informed estimates of retirement dates so that power plants can be treated as what they are – life span property. For reasons that are not apparent, the Staff, unlike the staffs in virtually all other jurisdictions, seems incapable of doing so and instead chooses to rely on an analysis its own witness admits is flawed, and that treats these power plants in contradiction to the manner in which every authoritative source says they should be treated.

Despite its own witnesses' testimony, the Staff, in its initial brief, is now manufacturing criticisms of the Black & Veatch study that no witness in this case testified about, and that are contradicted by the record.[91] Staff witness Rice on redirect mustered but one tiny criticism of the study: that *perhaps* "some attempt" to do an economic analysis at Meramec could have been

[88] Mr. Selecky: The study is "substantially better" than the manner of estimating retirement dates used by AmerenUE two rate cases ago, and it is a "better study by far." Tr. p. 1483, l. 19-23; p. 1485, l. 3-7.
[89] Ex. 108, p. 8, l. 1-6 (citing Rice Deposition, p. 110, l. 2-3). Note the circularity of the Staff's argument: the analysis is insufficient because an economic analysis wasn't done, but since an economic analysis can't be done, the life span approach can't be used leaving us, by default, with their admittedly flawed "true mass property treatment."
[90] Ex. 108, p. 8, l. 14-17.
[91] Staff's Initial Brief, p. 47.

made.[92] As noted, he admits such an analysis can't be done. In fact, the Staff's made-up criticisms are at odds with Mr. Rice's opinion and sworn testimony:

- "Overall, I believe the estimated retirement dates presented by [Company witnesses] Wiedmayer and Loos to be reasonable;"[93]
- He [Mr. Rice] spent "enough time and" has "enough knowledge to be able to understand Larry Loos' testimony and thought it well done."[94]
- "What Mr. Loos did is rational."[95]
- "What Black & Veatch done (sic) is relatively complete, logical."[96]
- The Black & Veatch study "is as reliable, or at least within a reasonable range of reliability, of what could be done today."[97]
- He does not "really have any criticism of what they (Black & Veatch) did given the limitations of trying to estimate the retirement of large steam units decades into the future."[98]
- "They did pretty much probably all they could."[99]

The Staff's rationale for stubbornly adhering to its flawed approach also continues to change in other ways, as reflected by statements at the beginning of the depreciation portion of the Staff's Initial Brief that purport to be based in fact, but which instead appear to be a collection of theories written by brief writers, but for which there is no support in the record. When Mr. Rice explained the assumption underlying the Staff's use (or attempt to use) a "true mass property" approach, he didn't claim the life span method is wrong because "the balance of plant [i.e., some steam plant components] tend to remain useful to the utility for very long

[92] Tr. p. 1444, l. 6-12.
[93] Ex. 168.
[94] Rice Deposition, p. 26, l. 25 through p. 27, l. 2.
[95] Rice Deposition, p. 68, l. 5.
[96] Rice Deposition, p. 110, l. 8-11.
[97] Rice Deposition, p. 110, l. 12-15.
[98] Rice Deposition, p. 110, l. 16-21.
[99] Rice Deposition, p. 110, l. 20-21.

periods of time . . .", as the Staff's Initial Brief claims. The record contains no such evidence, so not surprisingly, the Staff cites none.

Moreover, Mr. Rice didn't mention anything about a "not in my back yard" attitude or how it could allegedly cause the investment in these steam plants to "live on," as the Staff's Initial Brief also speculates. In fact, Mr. Rice said just the opposite, that is, that he believes the Meramec, Rush Island, Labadie and Sioux Plants will be "going away," "not living on," in the next 12 to 36 years.[100] Similarly, nowhere through three rounds of testimony did Mr. Rice claim (as the Staff's Initial Brief now suggests) that these steam power plants won't be shut down because there are all kinds of "amenities" at the sites.

The Staff's new (and unsupported) arguments notwithstanding, what Mr. Rice actually said in an attempt to support the Staff's treatment of these power plants as mass property was twofold. First, he said that under "true mass property treatment" *if* there is sufficient final retirement data; *if* the data is reasonable; and *if* a statistically significant analysis can be done, *then* the Staff's approach "should" lead to results that are close to the results derived from the life span approach.[101] But we know those conditions were not satisfied, or as the record indicates, those are all "big ifs" that don't hold true in this case.[102] Second, Mr. Rice claimed that if one uses an estimated retirement date that it could lead to a "fixed mentality" that might cause the utility to shut down a plant when it shouldn't do so,[103] but on cross-examination, Mr. Rice admitted that his contention was completely baseless; that it was "nothing more than pure speculation."[104]

[100] Ex. 168.
[101] Ex. 200, p. 104.
[102] Tr. p. 1383, l. 19-24; Tr. p. 1404, l. 6-15.
[103] *Id.*
[104] Tr. p. 1390, l. 10-13.

Yes, the life span approach assumes that each of the *steam power plants themselves* will, at some point, be shut down entirely.[105] In fact, everyone in this case agrees that is in fact a valid assumption. *See, e.g.,* Mr. Rice: "Overall, I believe the estimated retirement dates presented by [Company witnesses] Wiedmayer and Loos to be reasonable. Short of a reversal of the environmental movement, and/or a decade long economic depression, I believe these plant [sic] will be *slowly going away* over the next 12 to 36 years" (emphasis added).[106] *Cf.,* Mr. Selecky, who made the same assumption for his life span rates.[107] The NARUC manual and Wolf and Fitch make that same assumption. It's the same assumption made by state commissions across the country – virtually all of them according to Mr. Wiedmayer, and all of the roughly 20 states where Mr. Loos has testified. The Staff made the same assumption for the Callaway Plant. So what we have are the admittedly *invalid* assumptions in the Staff's analysis (that the retirement history is sufficient to produce an accurate, a "true" mass property result) versus a *universally accepted and recognized assumption* in AmerenUE's study: that these large steam plants will, in fact, shut-down; that they will "go away" in the future.

What the Staff is apparently trying to imply is that the bulk of what will then be 60 or 70 year old buildings and equipment will live on in some other form. But there's *no evidence* to support the Staff's speculation on that point either, and in fact there is evidence that contradicts it. For example, when the Staff's lawyer methodically tried to suggest that AmerenUE would just continue to use the steam plant components as part of some future operation of the Meramec Plant using gas, AmerenUE Vice President of Power Operations Mark Birk made it clear just

[105] It does not assume that one or more of these sites will no longer remain as nodes on the transmission system. The transmission investment at these sites is not at issue. It is unaffected by the *steam plant account* depreciation rates at issue here because the transmission investment is depreciated via depreciation rates applicable to the transmission accounts, which for the Company and the Staff are in all material respects the same. Nor does using the life span approach for the *steam plants themselves* assume the sites – the land – will be useless. No depreciation expense is being collected, or proposed, for the land on which these power plants sit.

[106] Ex. 168.

[107] "That *[life span] is the method I've used the most, yes sir*. Q. And that's the method that you think is more equitable; isn't that right? *A. Generally, yes.*" Tr. p. 1493, l. 7-11.

how unlikely that is, as the discussion of the *actual evidence of record on this point* appearing at pages 72 to 73 of the Company's Initial Brief demonstrates.

The Staff also claims that its approach "recognize[es] the capital necessary for the eventual retirement of the plant, and allow[s] recovery of that capital over the useful life of the plant."[108] That statement is simply not true.[109] Indeed Mr. Rice admits that an un-depreciated balance *will* remain:

> Q. And he told you that the mass property approach would not capture the short-lived equipment that remain in the plant when it retired and, in fact, he also told you that, in fact, if you do not have representative plants in your data, the mass property approach will not capture that short-lived property, will it?
>
> *A. That's what Mr. Wiedmayer said, yes*
>
> Q. And the problem Mr. Wiedmayer identified, in fact, does exist in this case, doesn't it?
>
> *A.* ***Yes*** *(emphasis in* ***bold****).*[110]

The Staff claims that there is an "inherent problem" with the life span approach, that is, *if* (again note the Staff's repeated use of this conditional language) the dates used for retirement are too early, then "current ratepayers could overpay, with no opportunity for recourse."[111] As support, they cite to Mr. Selecky's hearing testimony, but they are selective in their citation and take it out of context. The support the Staff cites was when MIEC counsel Downey was redirecting Mr. Selecky and discussing with him Mr. Selecky's admission that there is a "strong potential" that use of the mass property treatment for the steam plants will lead to an un-depreciated balance at the end of the life of the plant. Mr. Downey asked Mr. Selecky if there

[108] Staff's Initial Brief, p. 42. That this is true is further demonstrated by Schedule JFW-ER11 to Ex. 105, which shows that overall the *average* service life being used by the Staff for the steam production plants is 46 years, yet when taking interim additions and retirement activity into account, it is expected that the average service life will be much shorter – just 28.93 years (last column, bottom row of Sch. JFW-ER11).
[109] *See* the discussion of the record on this point at pp. 49 to 54 of the Company's Initial Brief.
[110] Tr. p. 1387, l. 7-18.
[111] Staff's Initial Brief, p. 44.

was a "possibility" that this could happen with the life span approach, and Mr. Selecky said "Yeah, if you don't adjust the lifespan. I mean, it's – the same thing could happen …."[112] But that "possibility" (not a likelihood, as the Staff's "inherent problem" statement implies) is at odds with the actual position of the Staff's "supporting" witness, Mr. Selecky, who agrees that the life span approach is more equitable (i.e., that the potential for over- or under-recovery is greater with the mass property approach):

Q. Would you turn to page 95 of your deposition, please?

A. *Uh-huh.*

Q. Page 94, actually, starting on line 16.

A. *Okay. Yes, sir.*

Q. Would you verify, please, that I'm reading these questions and answers correctly?

> "Question: But if in the next 25 or 30, 35 years, 40 years, we retire all four of them, we've been depreciating them using average service lives of 60, 70, 80, 115 years depending on the components, we're going to have an undepreciated balance related to those four plants that's going to have to be recovered, right? "Answer: That -- there is a potential for that, yes. "Question: A pretty strong potential, isn't there? "Answer: Yes. "And it's going to have to be recovered from ratepayers after those plants are retired from whom -- from whom -- and those ratepayers are not going to be taking any service from those plants, right? "Answer: Correct. "Question: And the ratepayers being served by those plants from today until my 30-, 35-, 40-year date, whichever, whatever you want to pick, whatever your pleasure, they will not have paid the entire service value of those power plants over the service lives of those power plants, will they? "Answer: That is a potential property -- problem with the whole life rates [mass property], definitely. "Question: **And it's a fairly significant problem with the whole life rates, isn't it? "Answer: It can be, yes.**" Did I read that accurately?

A. *You read that accurately.*

Q. **In your opinion, in fact, it's more equitable to estimate a date when each plant is going to be retired and depreciate it based on that date, and as you point out, every three to five years update your**

[112] Tr. p. 1544, l. 18 to p. 1545, l. 10.

depreciation study as opposed to using a 115-year average service life which assumes that at least one of these plants will last 230 years, correct?

A. ***That is the method I've used the most, yes, sir.***

Q. And that's the method that you think is more equitable; isn't that right?

A. ***Generally, yes*** *(emphasis in* ***bold).***[113]

Of course it is true that no method of depreciation – life span or mass property – will get the depreciation expense exactly right by the time the life of the plant ends if one sets depreciation rates at a given point in time and never again reviews the parameters (including the life spans).[114] But no one, least of all the Company, is suggesting we never look at the parameters again. What will happen, as discussed in the question Mr. Selecky answered above, is that every three to five years a new depreciation study will be done as required by the Commission's rules, and if retirement dates need to be adjusted, they will be. But as we pointed out in our initial brief (pages 51 to 54), there is insufficient retirement history, and there will likely continue to be insufficient retirement history, to allow use of the Staff's so-called "true mass property approach" to set depreciation expense with any reasonable level of accuracy for these large power plants, which to state the obvious again, are *not* mass property.

The life span approach produces *remaining life rates*; that is, the depreciation rate, every three to five years, is changed if needed so that if the retirement date estimate holds true the plant will be fully depreciated, no more and no less, on the day it retires.[115] If after three to five years updated analyses show the retirement date estimate should be shortened or lengthened, the

[113] Tr. p. 1491, l. 9 to p. 1493, l. 11.
[114] AmerenUE acknowledges that Meramec or any of the other plants could actually retire later, or sooner, than the current estimates. Staff Brief, p. 48. But AmerenUE would point out that its estimates are conservative (i.e., long – 61-72 years) when compared to those Mr. Selecky typically sees (around 60 years) and when compared to those being used currently for depreciation purposes for nearly 150 facilities in other states (approximately 55 years). This strongly suggests that the plants are more likely to retire sooner, not later, than currently estimated.
[115] Ex. 104, p. 37, l. 7 to p. 38, l. 13

remaining life rate will be adjusted. But with the mass property approach, and its use of "whole life" rates, the Staff is relying on an insufficient retirement history to set depreciation rates. AmerenUE will likely perform from two to five additional depreciation studies (as required by Commission rule) between now and the estimated retirement date of the Meramec Plant, yet the final retirement history that the Staff would use for its true mass property treatment in those studies will be even *less* sufficient as time goes on because it is likely that the total investment in the steam production plants will increase over time, yet there will be no more final retirement data available for study. This suggests Staff's method will become less accurate. The opposite should become true if the life span approach is used because as we move through time it stands to reason that the accuracy of the estimated retirement dates will improve.[116]

B. Mr. Selecky's recommendation to use the mass property approach for steam production, made in this case and this case alone, is flawed and should be disregarded.

"The Commission should continue to use the whole life [mass property] approach …"[117] While that has now apparently become MIEC's primary "recommendation" for the steam production plants, its own witness has never himself used that approach for steam production before. And it is particularly odd for MIEC to advocate for the mass property approach for steam production plants, when its witness agrees that steam production plants are not mass property; instead, a steam production plant and mass property are, to use Mr. Selecky's words, "different animals."[118] Moreover, his use of this approach is based on essentially the same flawed parameters as used by the Staff in Case No. ER-2007-0002, which the Staff itself deems

[116] Nor is the Staff's statement that the Company is using the life span approach to promote a "utility favorable level of annual depreciation expense" true. Adoption of the Company's depreciation expense in this case would put the Company at just approximately the 33rd percentile nationally, leaving the depreciation rates of two-thirds of other electric utilities at a higher level than the Company's rates. Ex. 105, Sch. JFW-ER8.
[117] MIEC Initial Brief, p. 16.
[118] Tr. p. 1480, l. 21-25.

unreliable.[119] Indeed, by ignoring what final retirement data for steam production plants that does exist, Mr. Selecky has in effect assumed the plants will live forever.[120] In addition, MIEC's entire approach to depreciation for the steam production plants, which if adopted would reduce *current* depreciation expense for those plants by nearly 13 percent, is completely at odds with Mr. Selecky's recognition, as stated in the NARUC depreciation manual, that depreciation rates *increase* for life span property as it ages.[121]

A review of the record in this case, as Commissioner Kenney's cross-examination of Mr. Selecky confirms, shows that Mr. Selecky's arbitrary decision to treat power plants as mass property in this case and this case alone is nothing more than an attempt to "play … to [his] audience," apparently hoping they would like the show, regardless of whether sound depreciation practices support either the method he used, or the parameters that he used in that method.[122] So what we have here is a case where for the steam plants, Mr. Selecky "plays to his audience," and for transmission and distribution plant, he "runs numbers up a flagpole." In both cases, it is obvious that his arguments rest not on sound analysis, but rather, are result oriented; that is, MIEC seeks to cut AmerenUE's depreciation expense to the bone (below the 10th percentile, to be exact) by any means possible.

This is further confirmed by Mr. Selecky's less-than-credible response to another question from Commissioner Kenney. Commissioner Kenney asked Mr. Selecky if he thought

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[119] Ex. 216, p. 6, l. 1 to p. 9, l. 4 (Rice rebuttal).
[120] Ex. 217, p. 8, l. 21 to p. 9, l. 2 (Rice surrebuttal). Consider for example that Mr. Selecky's mass property rates for steam production, which as noted use essentially the same unreliable parameters the Staff used two rate cases ago, include an *average* service life for the largest steam plant account of *115 years*, which implies a maximum life of *230 years* for one or more of these steam plants!
[121] Ex. 406, p. 12, l. 1-2 (Selecky surrebuttal). The 13% decrease is demonstrated by a comparison of Sch. AWR-3B to Mr. Rice's Surrebuttal Testimony (Ex. 217) and Mr. Selecky's Sch. JTS-15 (to Ex. 406). It is also noteworthy that the Company's proposed depreciation expense for the steam production plants, in dollars, in this case is only 7.5% higher than the depreciation expense for those plants was in 2001, when the investment in the steam plants was undoubtedly materially less than it is now. Mr. Rice's Sch. AWR-3B. The Staff's proposal would in fact reduce depreciation expense for the steam production below 2001 levels by more than 15%. *Id.*
[122] Tr. p. 1529, l. 1-25.

he was "employing the correct analysis" in treating these power plants as mass property, and Mr. Selecky said "yes."[123] We ask: how exactly can one square his claim that treating these power plants as mass property is "correct" with Mr. Selecky's admission that the life span approach is the approach he always used, and his admission that the life span approach is generally more equitable than the mass property approach? Can one reconcile this clear inconsistency because the retirement date estimates were poorly developed? The answer is "no." Mr. Selecky agreed that what Mr. Loos did to develop those dates is what he does and with one exception (the five-year shift for Meramec) Mr. Selecky in fact used Mr. Loos' dates for his alternative life span rates:

> Q. That 61 to 73 years, that's on the high end of what you've typically been seeing used for other utilities that are using the lifespan approach in the rate cases to set the depreciation rates, right?
>
> *A.* *I would say yes.*
>
> * * *
>
> Q. And in fact, the manner in which Mr. Loos and Black & Veatch went about in – in developing those dates, that's essentially what you yourself have done in the past, isn't it?
>
> *A.* *Something similar, yes.*
>
> Q. You agree that the Black & Veatch analysis was reasonable and logical, wasn't it?
>
> *A.* *It seems his approach was reasonable and logical, yes.*[124]

C. <u>The criticisms of the Black & Veatch estimates that appear for the first time in MIEC's Initial Brief are contradicted by the record.</u>

In its initial brief (see generally pages 20 to 25, in item 12i), MIEC supports its advocacy of using the mass property approach for property Mr. Selecky admits is a "different animal" by attempting to undermine the retirement date estimates developed by Black & Veatch in ways that

[123] Tr. p. 1529, l. 6-8.
[124] Tr. p. 1482, l. 16-21; p. 1483, l. 10-18

are contradicted by Mr. Selecky's own testimony, with one exception. In fact, MIEC's Initial Brief states that "they [the Black & Veatch estimates] are just as speculative now as they were in Case No. ER-2007-0002." MIEC's Initial Brief states that the Black & Veatch work is a "slick study" and claims it's not reliable.[125] But the hyperbole in MIEC's brief is at odds with MIEC's own witness's testimony:

Q. And the other – other than the life estimate for the Meramec plant which we'll talk about in a moment, you have no criticism of the dates and you have no problem with using them to set depreciation for AmerenUE steam plants, do you?

A. That's correct. That's what I used to develop lifespan rates.

Q. And in fact, the manner in which Mr. Loos and Black & Veatch went about in – in developing those dates, that's essentially what you yourself have done in the past, isn't it?

A. Something similar, yes.

Q. You agree that the Black & Veatch analysis was reasonable and logical, wasn't it?

A. It seems his approach was reasonable and logical, yes.

Q. And the manner in which Black & Veatch went about estimating lifespans of the steam plants **is substantially better than the manner UE went about doing so in ER-2007-0002, isn't it?**

A. I would agree with that, yes.

Q. And in fact, in that case, the ER-00 – or 2007-0002 case, in that case, UE's position on its estimates, particularly its first positions, was arbitrary, wasn't it?

A. I would say so, yes. And then all the years [plants] basically retired in the same year.

* * *

Q. But by contrast in this case, Black and Veatch analyze and took into account an orderly staging of replacement capacity where there wouldn't

[125] MIEC's Initial Brief, p. 24.

really be much overlapping construction to replace the retired capacity, correct?

A. *That was the intent of the Black & Veatch study, yes.*

Q. That's what –

A. *And that's what they did.*

Q. –what they did, right?

A. *That's what they did, right.*

Q. And that was a reasonable thing to do, wasn't it?

A. *Well, it – it – it seemed – it was* ***much more reasonable than the last case, there's no doubt about that****.*

Q. And in fact, there is a better study, to use your words, by far in this case respecting the proposed retirement dates than there was in that ER-2007-0002 case, isn't there?

A. *Yes,* ***it's a better study by far***.[126]

Little more needs to be said. MIEC can come up with new, unsupported statements about what their lawyers or principals apparently want the Commission to believe Black & Veatch should have done, but none of it matters given that their own witness didn't testify about any of these theories, and indeed he does essentially the same kind of study when he uses the life span approach (as he always does). None of these new, unsupported arguments matter when their own witness agrees the study was reasonable; where their own witness agrees the study is "better by far" than in Case No. ER-2007-0002. That statement alone proves conclusively that the claim that the retirement date estimates are "just as speculative" as those proffered by AmerenUE two rate cases ago is, to put it bluntly, false. To put the icing on the cake, their own witness also used

[126] Tr. p. 1483, l. 3 to p. 1484, l. 4; p. 1484, l. 13 to p. 1485, l. 7 (emphasis in **bold**).

the Black & Veatch retirement dates (except he does argue that the Meramec retirement date should be extended by five years) in the life span rates he is sponsoring in this case.[127]

D. If mass property rates for steam production were to be used all final retirement data must be used, else the insufficiency of data problem (and the failure to provide sufficient depreciation expense) the Staff admittedly has will be even worse.

Not only did Mr. Selecky choose for the first time ever to calculate mass property rates for large steam plants, but as discussed earlier, he did so using essentially the same flawed parameters the Staff used in Case No. ER-2007-0002.[128] And, the Staff was very clear – those parameters are flawed because they ignore what one absolutely cannot ignore if one is going to attempt to treat life span property like a power plant as mass property. In short, Staff has a substantial sufficiency of data problem because what little final retirement history exists is insufficient, but Mr. Selecky's argument that even that final retirement history should be ignored renders his mass property analysis even less reliable than the Staff's.

Nonetheless, MIEC consumes four pages of its initial brief arguing that because the Mound, Cahokia and Venice I plants were old, inefficient units, one must ignore their final retirements in conducting a mass property study of power plants. MIEC even claims that because AmerenUE did not include this final retirement data in its study, it shows that MIEC's claim is correct. MIEC's reference to what AmerenUE did is misleading because AmerenUE conducted a *life span study*, and *did not* treat these power plants as mass property.

[127] MIEC's other "criticism" is that the estimated life spans would have three of the plants retired within a span of 13 years. MIEC Initial Brief, p. 22. It is undisputed that Black & Veatch considered the time needed between retirements to accomplish an orderly replacement of the capacity. In fact, the three plants at issue were all built within just *ten* years (Sch. LWL-E1, p. 1-3, to Ex. 107), demonstrating that retiring those three plants within a longer plan of time is entirely reasonable.

[128] Tr. p. 1487, l. 8-12; AmerenUE's Initial Brief, pp. 66-68.

AmerenUE did not include *final* retirement data in its study because a life span study, by definition, studies *interim retirements only*.[129] This is because the average service lives developed from studying the data in a life span study are used to predict the average service lives of *interim retirements*, not the *life span* of the plant and of the plant components that will be retired when the plant itself is retired. This is why the survivor curves in Mr. Wiedmayer's study are truncated at the point of the plant's retirement.[130]

But for a mass property study, there is *no distinction* between an interim and a final retirement – in fact, all of the retirements are treated as interim retirements – because the theory is that the account will live on forever.[131] As a result, if the final retirement data is ignored, the average service lives will be overstated (because the study fails to account for dollars when an individual plant is actually retired – i.e., since all retirements are interim, under this treatment, excluding part of the retirement history understates the retirement activity, and leads to average service lives that are too long). Mr. Rice properly characterized MIEC's attempt to exclude final retirements from the development of mass property rates as "misleading."[132]

For the reasons discussed earlier in this brief, and in the Company's Initial Brief , these power plants should not be treated as mass property, but if they are going to be treated as mass property, one *must* use all of the final retirement history that is available else the mass property rates will be even more incorrect than those already calculated by the Staff. To use the Staff's terminology, the lack of "true mass property treatment" will be even worse. Or as Mr. Rice put it, this "is equivalent to an assumption that individual steam production units [i.e., each Plant] will last forever, which is not true."[133]

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[129] Ex. 104, p. 16, l. 14-25.
[130] Final retirements are excluded from the life analysis when the life span approach is used. *Id.*
[131] Ex. 200, p. 103, l. 14-29.
[132] Ex. 216, p. 6, l. 3 to p. 7, l. 10.
[133] Ex. 217, p. 12, l. 1-2.

E. Mr. Dunkel's adjustment to mass property rates is improper.

It is obvious that MIEC is making the argument that the final retirements should be ignored to give credence to Mr. Dunkel's proposed $5.7 million adjustment to the *Staff's* proposed mass property rates for steam production.[134] Mr. Dunkel's argument is that one must exclude final retirement data from the mass property analysis to prevent there from being an allowance for what he terms as "terminal net salvage." The fatal flaw in Mr. Dunkel's theory is that as discussed earlier, inherent in the mass property approach is that fact that there is no distinction between "interim" or "terminal" (final) net salvage. To the contrary, all retirements are interim. As Mr. Rice explained, if you accept Mr. Dunkel's theory, for the entire part of the investment in all of the steam plants that will be retired when the plant itself is retired, there will be *no accrual for net salvage at all*, yet we know net salvage expense occurs:

> Q. What that means is, that Mr. Dunkel's proposal would leave a portion of the plant balance, a portion of the investment in those steam production plant accounts, a portion of that plant balance would have no accrual for net salvage at all if you followed his recommendation, right?
>
> *A.* *Correct?*
>
> Q. Is that appropriate in your view?
>
> *A.* *No.*
>
> Q. Won't there be some kind of net salvage cost associated with all of the plant, whether it be through final or interim retirement?
>
> *A.* *Correct.*
>
> Q. It isn't appropriate to have some of the portion – some portion of the account with no accrual for net salvage, is it?
>
> *A.* *In my opinion, no.*[135]

[134] MIEC's brief quantifies this adjustment at $5.8 million; Mr. Dunkel testified at the hearing that this number is wrong, and that he proposing a $5.7 million adjustment instead. Ex. 439; Tr. p. 1448, l. 17-24.
[135] Tr. p. 1427, l. 6-22.

In a mass property analysis, "salvage is salvage." To adopt Mr. Dunkel's argument will exacerbate the data insufficiency problem we have further. Not only will ignoring the final retirement history, as Mr. Selecky argues should be done, lead to unreasonably long average service lives (i.e., assume that the individual plants will live forever), but Mr. Dunkel's proposal will lead to a failure to collect net salvage on a part of the investment. For these reasons, if mass property rates were used, Mr. Dunkel's proposal must be rejected.[136]

F. The record does not support extending the life span estimate for the Meramec Plant by five years for the purposes of calculating life span depreciation rates.

In his direct testimony, Mr. Selecky cited two bases in support of his argument that if the life span approach is used the retirement date for Meramec should be 2027, not 2022. First, he argued that because the youngest unit at other AmerenUE plants, at the time of its retirement, will be five years older than the youngest unit at Meramec in 2022, then it should be assumed that Meramec will live five more years. We addressed this argument in our initial brief (pages 70-71), and MIEC makes no mention of it in any event in its initial brief. It suffices to say that to argue, as Mr. Selecky did, that the oldest, least efficient plant in AmerenUE's fleet will live longer than any of the newer, more efficient plants makes no sense.

Mr. Selecky's second argument is based on a study that arose out of AmerenUE's last Integrated Resource Plan which simply answers the question: *if* economics, and *if* environmental regulation allowed Meramec to continue to operate beyond 2022, how much money would AmerenUE have to spend to keep it in service? We addressed this argument in detail at pages 71

[136] As we will explain in a motion we intend to file relating to the RLJ's recent issuance of an order admitting the true-up reconciliation into evidence, an adjustment to Mr. Selecky's already-flawed mass property rates to account for Mr. Dunkel's separate adjustment (which Mr. Dunkel proposed to the *Staff's* rates only) is improper and not is not supported by *any* evidence of record and thus cannot be relied upon by the Commission. Mr. Selecky's depreciation expense recommendation is what it is; MIEC can't, through its brief, in effect amend or supplement the testimony of Messrs. Dunkel and Selecky, and indeed manufacture "evidence" of a different level of expense when in fact there is no such evidence in the record.

to 73 of our initial brief. In its initial brief, MIEC mischaracterizes this study. MIEC claims that it "determined that a number of options existed for retirement of the Meramec Plant." To the contrary, the study didn't consider at what point Meramec would be retired at all. Rather, as the study report indicates, the study simply answered the question of what dollars it would take, if economics and environmental regulations allowed it, to physically keep the plant running. Indeed, the study's expenditure recommendations "have been made from an engineering and feasibility perspective."[137] Neither environmental regulations nor the "potential financial impacts" thereof were factored into the analysis.[138] The study did not consider "the economic viability of the plant and any environmental regulations."[139] The study also recognized that extending the life of Meramec would be a challenge:

> The Department of Energy's EIA-860 report lists the oldest domestic coal-fired plant [sic] rated greater than 10 MW as Detroit Edison's Trenton Channel Plant, which was brought online in 1949. Comparatively, Unit 1 at Meramec was brought online in 1953. There are only 30 coal plants throughout the United States rated at 100 MW or greater older than Meramec 2. *This illustrates the unique challenge Meramec will face to continue operation through this retirement option or longer* (emphasis added).[140]

Importantly, overcoming this "unique challenge" would depend not just on whether economics and environmental regulation would justify continuing to operate Meramec beyond its 69 year age (as of 2022), but also on whether AmerenUE spent the huge sums of money this study said AmerenUE would have to spend to do so. As Mr. Birk explained, the study concluded that capital expenditures from 2009 to 2014 would need to be $50 million *per year* and $20 million per year thereafter, yet the Company during 2009 through 2011 has spent or plans to spend just $50 million *total* – or just about 1/3 of what it would need to spend.[141]

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[137] Ex. 438HC, p. 1-2.
[138] *Id.*
[139] Tr. p. 2753, l. 4-16.
[140] Ex. 438HC, p. 5-1 (the "retirement option" under discussion was a 2021/2025 option).
[141] Tr. p. 2753, l. 20 to p. 2755, l. 4.

MIEC's Initial Brief also contains an additional argument, that is, that AmerenUE may just turn Meramec into a gas-fired plant.[142] MIEC claims that "AmerenUE admitted" that a conversion from coal to gas would address most of the space and environmental concerns if the gas line could be expanded, and cited more than 16 pages of Staff Counsel Kliethermes's cross-examination of Mr. Birk during the hearing. As outlined in detail at pages 72 to 73 of the Company's Initial Brief, a conversion to gas is not under consideration, and is highly unlikely. Space considerations would not drive such a decision; economics would, and as Mr. Birk testified, the economics do not appear to be favorable.

G. The record supports the net salvage percentage used by the Company for Account 312.[143]

MIEC's other attempt to cut AmerenUE's depreciation expense for steam production if the life span approach is used relates to its arbitrary change to the net salvage percentage for the largest steam production plant account, Account 312. We addressed this adjustment in detail at pages 74 to 76 of our initial brief. The only point MIEC makes in its initial brief is to claim that AmerenUE's calculation was "not reliable" because it assumed 60% of the removals in this account would be from interim retirements.[144] MIEC claims that the 60% figure is inconsistent with statements elsewhere in testimony that place that percentage at 20 to 50%. As with most if not all of MIEC's claims (e.g., their claim that something "seems" to high; that sometimes various items are determined arbitrarily; that things "may not" be accurate), the claim that AmerenUE's calculation is "not reliable" isn't based upon analysis or a careful examination of the data, but rather, it's based upon taking a general statement that has nothing to do with the issue at hand, and that ignores the data and sound analytics that underlie the -15% net salvage percentage for Account 312.

[142] Mr. Selecky never so much as mentioned this in his testimony, either pre-filed or at the hearing.
[143] This adjustment is proposed if the life span approach for steam production is used.
[144] MIEC's Initial Brief, p. 26.

As outlined at pages 75 to 76 of our initial brief, for the account at issue, Account 312, the *actual data* shows that the percent of the investment in that account that will survive as of final retirement is 35%, which means that 65% will be retired via interim retirements. Mr. Wiedmayer used 60%, which actually tended to make his net salvage percentage *less negative* (resulting in less depreciation expense) than if he had used the 65% number.[145] Mr. Wiedmayer's general statement, which applied to all plants for which life span treatment was used,[146] was accurate and was not inconsistent with the actual ratio for the account to which Mr. Selecky seeks to make an adjustment. For six of these 10 accounts, for a "substantial portion" as Mr. Wiedmayer testified, final retirements are, according to the analysis, expected to account for between 50 and 80% of the investment, just as Mr. Wiedmayer indicated.[147]

H. The actual retirements of the steam generators at Callaway should not be ignored.[148]

Like his use of flawed parameters in his one-of-a-kind mass property recommendation for steam production, and his novel "offset" to depreciation expense applicable to transmission and distribution (T&D) facilities (which we address below), Mr. Selecky stands alone in arguing that actual retirements of equipment at the Callaway Plant should be *ignored* in determining the depreciation rates for the Callaway Plant. This argument is yet another case of Mr. Selecky ignoring substantial data present in the Company's property records and in effect making-up new deprecation rates based solely on nothing more than his own self-serving *opinion* of what a correct depreciation rate should be.

Mr. Selecky first argues the retirements were "not typical" and "dominate . . . the history." The facts belie this suggestion. In just the next five years alone, other major plant

[145] Using the 60% figure, and applying it to the actual experienced net salvage throughout the entire history of this account produces a net salvage ratio of -15%.
[146] Accounts 311, 312, 314, 315, 316 (steam production) and 321, 322, 323, 324, and 325 (nuclear).
[147] Sch. JFW-E1 to Ex. 104, pages A-2, A-5, A-10, A-13, A-16, A-20, A-22, A-24, A-26, and A-28.
[148] This adjustment is proposed regardless of which method is used.

components (nearly $50 million worth) will be retired at Callaway. For depreciation purposes, the plant is assumed to be in service for an additional 36 years (versus just 24 years of service to-date). Thus the approximately $80 million of steam generator retirements hardly "dominate" the history and do not skew the life or net salvage analyses. Moreover, most nuclear plants have had to replace their steam generators, making replacement typical.

Mr. Selecky makes two arguments in response. First, he claims the Company is "adjusting life analysis to include [future] retirements…."[149] Second, he claims that payments from Westinghouse were reimbursed retirements (i.e., that they were credited to these plant accounts; to the depreciation reserve). The record demonstrates that both contentions are incorrect.

The life and net salvage analyses conducted by both the Company and the Staff used data reflecting what *actually occurred* at the Callaway Plant. The $50 million of future retirements in the next five years was not considered and was not included in Mr. Wiedmayer's actuarial analysis. Rather, those facts simply illustrate Mr. Selecky's argument that approximately $80 million of retirements "dominate" the history is misleading given that over the life of the plant there will almost certainly be far more dollars of retirements. If one starts to selectively ignore actual data in these accounts, when over the life of the plant at issue the data will not dominate the history, one will "almost certainly overstate the remaining life calculations" and thus "artificially reduce . .. depreciation expense."[150] If depreciation expense is artificially reduced, then current customers will fail to pay their pro-rata share of the service value of the plant over its service life.

[149] Ex. 406, p. 11, l. 15-16 (Selecky surrebuttal).
[150] Ex. 105, p. 39, l. 10 to p. 40, l. 7.

The same problem exists with Mr. Selecky's artificial reduction of the net salvage percentage for this account to just -1.2%. The actual experienced net salvage percentage is -18%. The Company and the Staff both use -10%, because it is true that one needs to recognize that part of the retirements (estimated to be approximately 50%) will ultimately be final retirements, which are being covered by decommissioning trust fund collections from customers.[151] However, there is no basis to reduce that figure to just -1.2%, which would in effect accrue virtually no costs for future interim removals at the Callaway Plant at all. Mr. Selecky himself recognizes that as the plant ages interim removal costs will be higher.[152] Without accruing adequate net salvage to cover those costs throughout the plant's life, depreciation rates will have to artificially be raised later to make-up for the failure to properly accrue net salvage now. In fact, as outlined by Mr. Wiedmayer at p. 12, l. 21 to p. 14, l. 6 of his rebuttal testimony (Ex. 105), if Mr. Selecky's -1.2% net salvage ratio were used over the remaining life of the plant (36 years), interim net salvage accruals would total just 8.894 million of net salvage. The Company has already incurred about $32 million in net salvage, and is expected to incur an additional approximately $47.7 million over the remaining life of the plant. Consequently, Mr. Selecky's ultra-low -1.2% net salvage percentage would under-recover net salvage by at least $49 million.

The record also refutes Mr. Selecky's argument that Westinghouse payments are reimbursed retirements that must be taken into account in the depreciation analysis. As Mr. Rice's testimony (quoted in full at page 78 of the Company's initial brief) demonstrates, the

[151] 50% of -18% is -9%; the Company and the Staff rounded this figure to -10%.
[152] This is evidenced by his citation to the NARUC manual, which recognizes that depreciation rates increase over time, and his hearing testimony, where he acknowledges that net salvage percentages tend to become more negative over time. Tr. p. 1518, l. 20-22.

payments are not reimbursed retirements, which means they do not affect the dollars in the depreciation reserve (i.e., in accumulated depreciation).[153]

I. Mr. Selecky's changing offset to T&D net salvage is arbitrary, unsupported by the record, and is based on a flawed premise.

With regard to depreciation expense for T&D plant, Mr. Selecky's positions are like a moving target. In his direct testimony, he recommended $41 million annually for net salvage for T&D plant, which reflected a $35 million "offset" from the sum of net salvage he then believed was included in AmerenUE's depreciation rates. His $35 million offset would mean that the net salvage accrual in AmerenUE's depreciation rates would have been $41 million annually. But we know that his $35 million number was completely arbitrary, indeed, he just "ran it up the flagpole."[154] In surrebuttal, he changed his offset to $25 million, a figure no less arbitrary than the first, as we discussed in detail at pages 82 to 84 of our initial brief. That Mr. Selecky is simply guessing at what the net salvage component of depreciation expense should be is demonstrated by that fact that if there was any logic to (or analysis underlying) Mr. Selecky's position at all, he would have recommended a revised offset of just $12 million. This is because nothing had changed between the time he first recommended that the Commission allow a $41 million annual net salvage accrual (based on a $35 million offset) versus when he later totally changed his recommendation to just a $28 million annual net salvage allowance (based on a $25 million offset). In sum, Mr. Selecky's claim that an offset is needed at all, and that it should be $35 million or $25 million or $10, rests on no more analysis, and no more logic, reason, or evidence, than if he had thrown darts at a dart board.[155]

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[153] For example, nearly 60% of the dollars are fuel credits, which reduce fuel expense, including the net base fuel costs included in base rates against which changes in net fuel costs are tracked in the Company's FAC. See Ex. 130, p. 2, fn. 1 (Finnell direct).

[154] Tr. p. 1516, l. 12-24.

[155] MIEC suggests that since depreciation studies will be done periodically the Commission should just go along with his baseless figures, which could be "modified or eliminated" later if they turn out to be too low. MIEC Initial

MIEC's Initial Brief on this issue is noteworthy for what it does not mention. In supporting his contention that an offset was needed, in his direct testimony Mr. Selecky speculated that past inflation might not be a good predictor of future inflation; he claimed net salvage percentages can be determined arbitrarily; he emphasized the recent five- and 10-year expenditure levels for net salvage (associated with decades old plant that served far fewer customers); and he pointed to other state commissions (just four of them, to be exact) who do require that net salvage be expensed. We addressed each of these points in our initial brief.[156] But now, in its initial brief, MIEC's focus has shifted. Now, MIEC points exclusively to a $582 million accrual for interim net salvage over the *entire life* of these T&D accounts, the implication being (although they never come out and say so, because they have no idea that it is true) that this is too much – in Mr. Selecky's words: that it "seems excessive."[157] And to what do they point to confirm Mr. Selecky's feeling that this "seems excessive"? Nothing more than irrelevant comparisons to terminal net salvage for a nuclear plant. We also addressed the fallacies of these arguments in our initial brief.[158]

MIEC's last argument in support of Mr. Selecky's arbitrary and unsupported offset is that because future net salvage costs are projected to be materially higher than his historical average, then there must be some "question of the reliability" of the analysis upon which AmerenUE's net salvage expense is based.[159] Note that Mr. Selecky doesn't actually allege any flaw; he conducts no analysis to show any flaw, but rather, he appears to just be running the idea that there *could*

Brief, p. 32. AmerenUE has provided substantial and competent evidence, not speculation, that its net salvage estimates were based upon actual, sound analysis of the T&D accounts, and that net salvage costs in the future will become more and more negative, as cost of removal is inflated and as the much larger universe of plant serving customers today is retired. The Staff agrees. The T&D rates calculated by the Company and the Staff were calculated exactly in accordance with this Commission's policy. There is no substantial and competent evidence in this record upon which to base adoption of Mr. Selecky's arbitrary "offset," and the same should be rejected.

[156] See generally, pages 84 to 89.

[157] Ex. 406, p. 16, l. 14.

[158] Page 85.

[159] MIEC Initial Brief, p. 32.

be a flaw up the flagpole. This argument is simply a different way of casting the argument that is central to Mr. Selecky's attempt to cut AmerenUE's T&D depreciation; that is, Mr. Selecky wants this Commission to set net salvage accrual based upon an examination of historical average expense levels associated with the retirement of a much smaller universe of plant in the past.

The Commission has soundly rejected that idea, and we know the idea is fundamentally flawed because the dollar investment in AmerenUE's T&D system today is nearly 19 times more than it was in 1960, and the T&D assets serve more than twice as many customers now than it did in 1960.[160] Mr. Selecky agrees it is not at all surprising that the future expense is much higher than the past, but that doesn't seem to deter him from continuing to make the argument.[161]

In contrast to Mr. Selecky's supposition, the Company's net salvage accruals are based upon a detailed study of actual Company data covering a span of nearly 50 years.[162] The study is in two parts, a life study and a net salvage study. The life study, the results of which are depicted on the appropriate survivor curve for Accounts 364 and 365 (see pages A-94 and A-98 of Schedule JFW-E1 to Ex. 104), produces an average service life of poles in Account 364 of 45 years and of overhead conductors in Account 365 of 49 years. The net salvage analysis, also based on actual data collected over many decades, reflects a net salvage analysis of -152 percent (Mr. Wiedmayer used -150%) in Account 364 and of -55% (Mr. Wiedmayer used -53%) in Account 365 (see pages B-70 and B-73 of Schedule JFW-E1). Those facts – derived from actual analysis of actual data over a very long period of time – are the bases for the projected

[160] Ex. 105, Sch. JFW-ER16.
[161] Tr. p. 1517, l. 15 to p. 1518, l. 22.
[162] The Staff's study is, in all material respects, identical, and the Staff arrived at very similar results.

retirements depicted in Mr. Wiedmayer's Schedule JFW-ER15,[163] figures from which Mr. Selecky uses in his Schedule JTS-12.[164]

Mr. Selecky can speculate all he wants about whether the average service lives and net salvage percentages are right or wrong, but the bottom line is that he conducted no independent analysis whatsoever that demonstrates that there is anything wrong with them. The average service lives and net salvage percentages used by the Company and the Staff are similar. They were derived from the same kind of analysis of actual data used in 46 of the 50 states, and from the same analyses repeatedly sanctioned by this Commission. They suggest net salvage percentages will become more and more negative over time – Mr. Selecky agrees that this is true; and they suggest that net salvage expense will grow over time – Mr. Selecky also agrees this is true. Mr. Selecky's adjustment to the Company's (and effectively, the Staff's) T&D depreciation expense is not supported by competent and substantial evidence and should be rejected.

III. COAL-FIRED POWER PLANT MAINTENANCE EXPENSE.

A. When the test year level of an expense is reflective of a reasonably expected level of expense once rates are set, it should not be "normalized."

A review of the Staff's Initial Brief regarding coal-fired power plant maintenance expense confirms that the Staff is proposing to normalize an expense that should not be normalized. It should not be normalized because the test year level of the expense *is* representative of the expected level "during the future period when rates will be in effect."[165] Ignoring the test year level of this expense means that the Staff is *not* employing the test year "as

[163] Ex. 105, Sch. JFW-ER15.
[164] Ex. 406, Sch. JTS-12.
[165] *Re: KCP&L et al.*, Case Nos. ER-81-42, ER-80-48, 43 P.U.R.4th 559 (Jun. 17, 1981).

a vehicle upon which to project experience [the test year] in a future period when rates determined in the [this] case will be in effect."[166]

Staff's first argument is that the test year level is "not representative" of a normal level.[167] The Staff cites no support for this contention, because there is none. The test year level is not consistent with backward-looking historical averages of expense in the early 2000s (when a dollar was worth far less than it is today) or from 2005 to 2009 (when far fewer than normal maintenance outages were being taken), but it *is* representative of the expense level one can reasonably expect during the time when rates will be in effect.

Staff's Initial Brief next contains an assertion that the Staff's own witness's testimony contradicts. The Staff's Initial Brief states that its recommendation "considers the newly extended planned outage cycle approved by AmerenUE management."[168] But that statement is not true because Ms. Grissum indicated that she gave *no consideration* to when outages occurred or how many outages there had been:

> Q. And you don't really know anything about the comparability between an outage in '03 and an outage in '08, do you?
>
> *A. No. I looked at* ***total dollars in an aggregate*** *as to what Company spent and performed a normalization ….*
>
> * * *
>
> *A. I'm not looking at outages and I have made no analysis as to whether there's abnormally low outages or not. I've not looked at that.*
>
> Q, Let me ask my question again because I don't think you answered it. Isn't it true that you may be using information from a three-year period during which the number of outages the Company – the number of scheduled, planned outages of the Company's plants is abnormally low?
>
> *A. I* ***do not know because I did not . . . look at outages*** (emphasis in **bold**).[169]

[166] *State ex rel. Missouri Power & Light Co. v. Pub. Serv. Comm'n*, 669 S.W.2d 941, 945 (Mo. App. W.D. 1984).
[167] Staff's Initial Brief, p. 51.
[168] *Id.*
[169] Tr. p. 1189, l. 13-18; p. 1190, l. 5-16. See also AmerenUE's Initial Brief, pp. 100 to 101.

The Staff then tries to bolster its mechanical use of backward-looking historical averages during an abnormal period by stating that in the past several years power plant maintenance expense was never more than it was in 2008 (which encompasses nine months of the test year).[170] What this "point" ignores is the undisputed fact that a dollar in 2008 or in 2010 is worth a lot less than a dollar in 2001 to 2003. What this point also ignores is that the reason the expense level was higher in 2008 is that the transition period was over and the Company was back to taking more outages – two major outages plus two "mini" outages – causing the expense level to, predictably, be higher than a simple historical average would suggest.[171]

The support for the Staff's position is so weak that the Staff has now resorted to the completely unsubstantiated suggestion that there was something untoward about the Company's extension of its outage cycles (and deferral of outages in 2009, due to the global financial crisis).[172] To that claim, we must ask: what is the Staff talking about? No one disputes that during the latter half of 2008 and in 2009 the country faced a financial crisis not seen since the early 1930s.[173] As far as extending the intervals between outages is concerned, there is not a shred of evidence in the record to suggest manipulation or imprudence or any other manner of unwise or improper conduct relating to the decision to extend those outages. To the contrary, the only evidence on that point is that it has saved money and resulted in more generation (which leads to more off-system sales, which in turn benefits customers):

> In approximately 2003, the Company determined that it could likely maintain a high level of equivalent availability at its coal-fired units while also extending the interval between major planned outages from an historic 18-24 month interval to intervals of three to four years, depending on the unit (the cyclone units at the Sioux Plant require more frequent planned outages). As the Company continued

[170] Staff's Initial Brief, p. 51.
[171] We discuss this issue at pp. 96 to 98 of our initial brief.
[172] Staff's Initial Brief, p. 52 (claiming "manipulat[ion]").
[173] One need only to read AmerenUE witness Lee Nickloy's direct testimony (Ex. 114) to understand the liquidity problems this crisis caused. Mr. Birk also testified that "there was a concern that we would not be able to get the adequate capital to be able to execute outages in '09." Tr. p. 1049, l. 9-11.

> to study the issue, it determined that it could extend those intervals even further like most of the industry was doing, to approximately six years between planned outages. Lengthening these outage cycles allowed us to maintain a high level of equivalent availability on the fossil units while absorbing a significant portion of the material and labor cost increases we were seeing associated with overhaul work throughout the last five years. The maintenance expenses at issue are driven to a great extent by O&M incurred in connection with planned outages.[174]

As addressed at page 98 of the Company's Initial Brief, the number of outages was literally at its lowest point in the past 10 years during two of the three 12-month periods the Staff used to develop its historical average (1.3 per year). The level of maintenance expense associated with that low level of outage activity will not support the level reasonably expected when rates are in effect (approximately 3 to 3.5 outages per year in 2010 and 2011).[175] Consequently, "normalization" is improper, because the test year level does reflect a normal level of expense during the period when rates will be in effect.

B. <u>MIEC's recommendation also fails to reflect an ongoing level of expense.</u>

After also (like MIEC witness Selecky) apparently just running a number up the flagpole in his direct testimony, MIEC witness Greg Meyer completely changed his approach in his surrebuttal testimony and has ended up with a new recommendation that is slightly higher than the Staff's final recommendation, which itself has changed.[176] As thoroughly explained in the Company's Initial Brief (pages 104 to 107), Mr. Meyer's recommendation makes no attempt to

[174] Ex. 102, p. 14, l. 3-13 (Birk rebuttal).

[175] Staff's contention that the 2010 budget should be ignored should be rejected. No party disputes the fact that an outage has already occurred in 2010 at the Meramec Plant, another outage was already underway at one of the Company's largest plants, Rush Island, at the time of the hearings in this case, and another major outage on two of the units at the Sioux Plant must be taken in connection with putting the scrubbers into service either late this year or in early 2011. As Mr. Birk testified, he is at a point where he "cannot go much longer" on taking these major outages and is "90 to 95% sure" that he will take a total of at least six major outages in 2010 – 2011, when rates set in this case will be in effect. Tr. p. 1007, l. 24 to. p. 1008, l. 7; p. 1052, l. 9 to p. 1053, l. 7; p. 1054, l. 17 to p. 1055, l. 15.

[176] Mr. Meyer recommends $105 million (versus his original recommendation of approximately $91 million); the Staff is now recommending approximately $104.1 million (versus its initial recommendation of approximately $101.1 million).

account for inflation, although many of the data points he relies upon use dollars from several years ago.

In its initial brief, MIEC points to 2013, 2014, and 2015[177] and tries to make the point that perhaps AmerenUE will not be taking three or more scheduled outages in those years, which MIEC would argue, shows that a level of expense from the test year (when two major outages and two mini-outages were taken) and in 2010 and 2011 (when rates are likely to be in effect from this case) is not a representative level of expense over the long-term. If the period during which rates are likely to be in effect from *this* rate case included 2013 and beyond, the MIEC's argument would have *some* validity (although at a minimum, inflation would need to be accounted for), but on this record, MIEC's argument is a red herring. There will be another rate case by the end of this year, which means there will again be new rates no later than late 2011. Consequently, the Commission is not setting rates for 2013 and beyond in this case. What may happen then is irrelevant.[178]

The second point MIEC makes then contradicts its first point. As just discussed, MIEC points to the future – three to five years in the future – and argues that this shows that the test year level may not be representative of maintenance expense in 2013 to 2015. The only future period that is relevant is 2010 and 2011, when rates will be in effect from this case. Yet MIEC argues that Mr. Meyer's surrebuttal analysis (touted by MIEC as producing a result close to AmerenUE's 2010 budget, which is very close to the test year sum)[179] is accurate, although it produces a recommendation of just approximately $105 million. But the record strongly

[177] MIEC Initial Brief, p. 4.
[178] In any event, MIEC's premise is wrong. MIEC's Initial Brief (at the top of page 6) contains a suggestion that there will be no outages in 2013. Mr. Birk specifically testified that the contention that there will not be outages in 2013 is incorrect. Tr. p. 1021, l. 11-13.
[179] The 2010 budget is $117.5 million versus a test year sum of $118.9 million, a difference of just 1.2 percent.

suggests $105 million is an *insufficient* level of expense to maintain these power plants in 2010 and 2011, as addressed earlier and in our initial brief.[180]

Mr. Meyer's methodology is not accurate for at least three reasons. First, as discussed in our initial brief, it makes absolutely no sense to use un-inflated dollars from as far back as 2004 to predict power plant maintenance expense in 2010 and beyond. A dollar now is indisputably worth less than a dollar then. Inflating those dollars using a conservative interest rate raises Mr. Meyer's analysis results to $113 million.[181] Second, some of Mr. Meyer's inputs are wrong. For example, Mr. Birk testified that the dollars Mr. Meyer was using for outage-related maintenance expense for a Rush Island outage (Rush Island is one of the Company's largest plants) is incorrect.[182] Third, the principal period of time examined by Mr. Meyer was from 2004 through 2009 when an abnormally low number of outages were being taken (in fact 13 of his 18 data points were from 2004 through 2009).[183] This is why, as MIEC points out at the bottom of page 7 of its initial brief, that "AmerenUE's base expenditures remained flat between 2005 and 2009." Indeed, the fact that the expenditures remained relatively flat during this period proves the Company's point – when outages are not being taken, or are taken less often, the expense is materially lower. During the historic periods used by Mr. Meyer (and the Staff), less outages were being taken, but this is simply not reflective of the conditions the record supports will exist when rates set in this case take effect.

[180] Tr. p. 1008, l. 2-7.
[181] Ex. 158, p. 4, l. 6-9 (Birk supplemental). MIEC's tortured attempt to manipulate the numbers during the hearing to "produce" a predicted level of expense near the 2010 budget does not change the fact that Mr. Meyer used dollars from earlier periods and failed to account for inflation in doing so.
[182] Tr. p. 1010, l. 18 to p. 1012, l. 1.
[183] Ex. 162HC. From 2005 to 2008 – about 1.91 outages per year; in 2009, just 1 outage – versus 2001 to 2004 – 3.5 per year, and 2010-2011 – also 3.5 per year.

IV. NUCLEAR FUEL COSTS.

The Staff's Initial Brief regarding the level of nuclear fuel expense to be included in base rates in this case contains not a single citation to any evidence of record in this case. It remains undisputed that the nuclear fuel costs will be higher by approximately $11 million before rates take effect in this case. In fact, no one has taken any issue with the accuracy of any of AmerenUE witness Randall Irwin's testimony. MIEC's argument consists of nine lines that makes a couple of the same points as made by the Staff, also without citation to any evidence. We addressed each and every point raised by the Staff and MIEC in our initial brief (pages 108 to 113). We offer the following abbreviated, additional comments here.

The Staff's entire argument boils down to this: their contention that there is a line-in-the-sand[184] at the true-up cutoff date and their plea that the Commission not go "down a path" that would reflect an admittedly known and measurable high level of costs *that will in fact be incurred before rates take effect in this case*.[185] Never mind that no one – not the Staff and not MIEC – opposed doing the very same thing in the Company's last rate case.[186]

The *only* other justification Staff proffers is that allowing the higher nuclear fuel costs will "surely" skew the relationship between rate base, expenses, and revenues.[187] MIEC makes no such claim. Staff cites no support in the record for this statement, because there is none. In fact, we demonstrated why that statement is not true in our initial brief – indeed, as the quote on page 112 of our initial brief indicates, Ms. Grissum *admits* that the only change that will occur is

[184] Tr. p. 2659, l. 15-19.
[185] As MIEC points out, the refueling will be complete in mid-May.
[186] It's obvious that neither the Staff nor MIEC care much about accurately rebasing the Company's net fuel costs now that the Company has an FAC, and now that it's likely that net fuel costs will rise, resulting in an automatic disallowance of higher fuel costs, including these higher nuclear fuel, without any showing whatsoever of imprudence on the Company's part. That disallowance will be at least 5%; if MIEC were to get its way, it would be 20%.
[187] Staff's Initial Brief, p. 55.

the nuclear fuel cost itself.[188] And this is obviously true because the relationship at issue is a proxy for what the Commission has determined is the relationship that is expected to persist *starting in mid-June when rates take effect*. This fuel will be in the reactor and will be producing electricity at that time; thus the relationship is preserved.[189]

The question for decision is this: does the Commission take the Staff at its word and do what the Staff claims should be done, that is, insist that all parties do the best job possible to rebase net fuel costs accurately, whether or not a utility has an FAC, or does the Commission let the Staff pick-and-choose when it does the "best job possible"? One thing about which we do agree with the Staff is the fact that the Callaway Plant is unique. We know that every 18 months it will be refueled. If we know the cost of the nuclear fuel assemblies that will be loaded into the reactor, and if that reload will be done before new rates in a rate case take effect, then the new costs should be included, whether they are higher or lower.

V. VEGETATION MANAGEMENT/INFRASTRUCTURE INSPECTION.

Both Staff and MIEC oppose the continuation of AmerenUE's trackers for its vegetation management and infrastructure inspection programs, both citing many of the same arguments. Both Staff and MIEC ignore the fact that many of these arguments were addressed by the Commission in AmerenUE's previous rate case. The facts which justified that order have not changed and the Commission should continue both trackers.

[188] Ms. Grissum testified inconsistently on this point at the hearing, claiming that including the fuel would upset the matching, yet during her deposition, before she had time to apparently consult with other Staff members, she told a different story: "Question: If that's true, then including Mr. Irwin's price in the Staff's modeling is not going to upset the matching of revenues, expenses and rate base, is it? Answer: I don't believe it will." Tr. p. 2671, l. 21-25. As noted, she went on to admit during the hearing that including the nuclear fuel costs won't affect the Company's O&M costs, won't affect capital investments (rate base), and that the only change that will take place to revenues, expenses, and rate base is the nuclear fuel cost itself. Tr. p. 2672, l. 3-25.

[189] And that is why, as we also pointed out in our initial brief, the Commission has, for example, included higher wages under labor contracts where the higher wages take effect *after* the true-up cutoff date, but before rates take effect. Company's Initial Brief, fn. 294.

Initially, both Staff and MIEC argue that AmerenUE has enough experience with these programs to use the test year's level of expenditures. This issue was discussed in-depth in the Company's Initial Brief.[190] AmerenUE provided the only witness with actual, operational knowledge specific to AmerenUE's vegetation management and infrastructure inspection programs.[191] The witnesses who testified on behalf of Staff and MIEC on this issue admitted on the stand that they did not examine AmerenUE's facilities or programs.[192]

Instead of analyzing AmerenUE's actual experience, both Staff and MIEC assert that because the current rules have been in effect for over a year, there must be a sufficient basis upon which to base rates.[193] But there are many elements to AmerenUE's experience that are not considered by this timing argument, and failure to consider those elements is the fatal flaw in the Staff's and MIEC's argument. The Commission's rules imposed many new requirements for AmerenUE's vegetation management and infrastructure inspection programs. For example, the amount of vegetation that must be removed when trimming vegetation around a line has increased significantly.[194] So the fact that AmerenUE had been working toward trimming on a 4/6 year cycle prior to the rules does not mean it knows what it will cost to trim under the Commission's rules on a 4/6 year cycle. Mr. Wakeman's written testimony demonstrated that AmerenUE had not trimmed half of its urban circuits or two-thirds of its rural circuits, leaving 60% of its total circuit miles that have never been trimmed under the new, Commission-imposed standards.[195] The percentage of facilities inspected under the infrastructure inspection rules is even smaller. As of February of this year, 78% of the Company's underground facilities and

[190] AmerenUE's Initial Brief, pp. 115-119.
[191] *Id.* p. 115.
[192] Tr. p. 1739, l. 21 to p. 1741, l. 21; Tr. p. 1757, l. 11-16; Tr. p. 1776, l. 9-15.
[193] Staff's Initial Brief, p. 67; MIEC's Initial Brief, pp. 12 and 14.
[194] Tr. p. 1737, l. 6-23; Ex. 110, p. 3, l. 21-22; Tr. p. 1737, l. 13-16; Tr. p. 1761, l. 11-18.
[195] Ex. 109, p. 7, l. 15-20.

70% of the Company's streetlights had not been inspected under the Commission's rules.[196] Further, when one examines the Staff's statement that AmerenUE's programs have remained constant over the past two years,[197] it is clear that Staff's witness was not saying that expenditure level had remained constant. The exact testimony at hearing was as follows:

> Q. [by AmerenUE's attorney] You say, the vegetation management program has essentially remained constant for at least the last two years?
>
> *A. That's correct.*
>
> Q. What two years are you referring to?
>
> *A. 2008 and 2009.*[198]

Several questions later in this sequence, Mr. Beck admitted that when he said the program was constant, he was not referring to the dollars spent on the programs.

> Q. And that was a step increase from the amount that had been expended prior to that point?
>
> *A. I believe it was both a step increase of the 45 million and the amount that was incurred prior, yes, both.*
>
> Q. So when you say that the program was remaining constant, you're not really talking about the dollars being expended, right?
>
> *A. That's - - that's correct.*[199]

This admission further supports AmerenUE's contention that while it is satisfying the requirements of the Commission's vegetation management and infrastructure inspection rules, it does not mean that the cost of this compliance is at a point where it is known or stable. Given those facts, there is no legitimate basis to believe that AmerenUE's programs have reached full maturity and no reason to deny AmerenUE's request to continue these trackers.

[196] *Id*. p. 9, l. 2-5.
[197] Staff's Initial Brief, p. 67.
[198] Tr. p. 1762, l. 20-25.
[199] Tr. p. 1764, l. 3-11.

Staff and MIEC also both argue that forecasted numbers aren't known and measurable and that it is unreasonable to rely on AmerenUE's forecasts.[200] In another portion of its brief, MIEC argues that trackers are appropriate only when expenditure levels are unknown.[201] Of course, these arguments and the argument above (AmerenUE has sufficient experience) are contradictory positions and cannot both be true. Either AmerenUE has enough experience to know what its costs for these programs are going to be or it does not. AmerenUE lacks sufficient experience, justifying continuation of these trackers. The Commission has already considered whether or not it was appropriate to rely upon estimated costs in the Company's last rate case when it established these trackers. The conclusion was that it was appropriate. There has been no change in circumstances which would justify a different conclusion today.

Staff also asserts several arguments in which they draw incorrect conclusions, conclusions which are directly refuted in the record. First, Staff quotes a portion of the Commission's vegetation management and infrastructure rules and claims that the rules don't allow for a tracker to continue past the first rate case.[202] AmerenUE is not relying upon the language of the vegetation management rule or the infrastructure inspection rule and does not need to rely upon that language in order to have these trackers, as admitted by Mr. Beck at the hearing.

Q. Does the rule prohibit the Commission from authorizing a tracker that varies from what's described in that language?

A. No, it does not.

Q. Okay. Does the rule prohibit the Commission from authorizing any specific treatment that it may desire to authorize?

A. No, it does not.[203]

[200] Staff's Initial Brief, p. 68; MIEC's Initial Brief, p. 15.
[201] MIEC's Initial Brief, p. 13.
[202] Staff's Initial Brief, p. 65.
[203] Tr. p. 1766, l. 4-11.

There is no reason to believe the Commission does not have the authority to grant AmerenUE a tracker in this case. Consequently, Staff's argument should be rejected.

Next, Staff argues that AmerenUE couldn't identify how much data was necessary before the tracker should stop.[204] Whatever the words "how much data" means, Mr. Wakeman's testimony was that he did not believe these trackers should be indefinite and that, as an example, he thought it would be appropriate to discontinue the vegetation management tracker in another two to four years as the Company would then have a full cycle of experience.[205]

Staff also argues that AmerenUE never proposed how to handle the over-collection, some of which was due to the accidental inclusion of internal labor costs in the initial estimate[206] and some of which is due to the fact that AmerenUE cannot, as of yet, be comfortable that it knows what it will cost to perform the additional work required by the Commission's rules. Regardless of how Staff would like to color the answer, Mr. Wakeman directly assured the Commission that the Company was not "going to put that money in its pocket," but rather that it should be an offset in the tracker just as an under-collection would be offset.[207] Additionally, AmerenUE's position is clearly set forth in its initial brief, where it stated:

> As noted, AmerenUE collected more than it spent during the first year of these trackers, so the Company requests the Commission offset this over-collection with the amount accumulated in a regulatory asset between October 1, 2008 and February 28, 2009. That leaves an over-collection in the amount of $3.4 million. AmerenUE agrees that if the Commission continues the trackers, it should also credit that amount back to customers, amortized over three years, just as it amortized the amount under-collected between January 1, 2008 and October 1, 2008.[208]

[204] Staff's Initial Brief, p. 69.
[205] Ex. 109, p. 7, l. 20-24.
[206] *Id.* p. 5, l. 12-21.
[207] Tr. p. 1721, l. 25 to p. 1722, l. 8.
[208] AmerenUE's Initial Brief, pp. 119-120.

Finally, Staff's Initial Brief asked the Commission, assuming it re-authorized these trackers, to impose the same 10% cap it placed on the trackers previously (in Case No. ER-2008-0318). AmerenUE does not object to that condition, as long as it allows the Company the option of coming to the Commission for an Accounting Authority Order (AAO) if it finds it must spend more than the 10% cap, just as the Commission ordered previously.[209]

VI. STORM RESTORATION TRACKER.

As AmerenUE pointed out in its initial brief, the Company recognizes it is asking the Commission to approve different treatment for the cost of restoring service to our customers after a major storm. The briefs submitted by the Staff and MIEC point out that AmerenUE can currently ask for an AAO and that the Company has often times done that. But the briefs filed by the Staff and MIEC miss the point of AmerenUE's request. The point is that the Company needs the Commission to take a step to reduce the excessive regulatory lag and the related cash flow problems associated with storm restoration costs.

As the Staff and MIEC correctly point out, the Company can ask for an AAO, which is typically amortized over five years.[210] Or, if the storm occurs during a rate case test year, the Company does not have to request an AAO and costs are amortized over five years.[211] As detailed in AmerenUE's Initial Brief, the Company currently has multiple (five) amortizations related to storm restoration costs and, to finance the cost of one restoration effort, sold SO_2 allowances.[212] The fact it has been necessary to take these measures over and over is, in and of itself, enough to demonstrate that the current method of determining what amount should be included in AmerenUE's revenue requirement is inadequate and should be changed. AmerenUE has experienced severe storms almost every single year and these storms require significant

[209] Case No. ER-2008-0318, Report and Order, p. 40.
[210] Staff's Initial Brief, p. 56; MIEC's Initial Brief, p. 10.
[211] Ex. 202, p. 2, l. 5-11 (Rackers rebuttal).
[212] AmerenUE's Initial Brief, p. 121; Ex. 200, p. 90, 1. 17 to p. 91, l. 21.

expenditures to restore service to our customers. In fact, Staff's own testimony shows that AmerenUE has spent more than nine million dollars on non-labor O&M to restore service after a major storm in three of the last four years.[213] Despite this fact, in every rate case, Staff proposes a removal of the costs of major storms and then normalizes the remaining costs so that, by definition, the amount put into AmerenUE's revenue requirement cannot be sufficient to compensate the Company for its major storm restoration efforts.[214] This forces the Company to recover storm restoration costs through a five-year amortization period, which unnecessarily drags out cost recovery and imposes excessive regulatory lag upon the Company.[215] A storm tracker, with a base set at $10.4 million, the actual test year amount, provides a solution that reduces the regulatory lag imposed by the current practice while protecting customers in those instances where the actual costs incurred by the Company do not rise to the level included in rates.

Staff and MIEC both make the argument that AmerenUE's vegetation management program will cause the Company to experience a reduction in storm restoration costs.[216] If true, the reduction will be captured by the tracker. However, this is not a likely outcome. This issue was discussed by Mr. Wakeman when he was on the stand, answering questions from Chairman Clayton. MIEC selectively quoted portions of this discussion but edited out a sentence which completely contradicts their argument. That section of the transcript is reprinted here with the inappropriately removed sentence in bold, for ease of comparison.

> If you are asking me [Mr. Wakeman] today, if the [vegetation management] standards were in place today or were in place then [2006] that are in place today, would it have made a difference? I think it would have made a difference. **I don't know if we would have seen a step change in the response for our**

[213] Ex. 203, p. 6, l. 6 (Rackers surrebuttal).
[214] Ex. 202, p. 2, l. 21-24.
[215] Ex. 110, p. 6, l. 7-10.
[216] Staff's Initial Brief, p. 62; MIEC's Initial Brief, p. 8.

system, but there would certainly in my estimation have been some outages that hadn't occurred, absolutely.[217]

Significantly, just prior to this point in the hearing, the following exchange occurred between Mr. Wakeman and Chairman Clayton:

Q. [I]s there a correlation between—between vegetation management and infrastructure expense and storm expense? Meaning you increase expense on the vegetation management side, does that correlate to lower storm recovery costs…?

A. I think it certainly can. I think it – it depends on the kind of storm. When you look at the storms we had in 2006 where huge trees were uprooted and blown into lines, that's not a tree trimming or vegetation management issue. But when you look at storms that occur more on the every day basis, 30, 40 mile an hour winds that can cause limbs to break off trees and fall, and then I think it does make a difference.[218]

Mr. Wakeman draws a clear distinction between the work required after a day-to-day storm and that required after a major storm, a distinction that Staff has ignored and that MIEC has attempted to obfuscate through its selective quotation of the record.

MIEC's Initial Brief also makes the argument that AmerenUE's improvements in its storm restoration practices will cause a decrease in storm restoration costs.[219] This assertion is completely unsupported in the record. First, the citation to the record to support MIEC's claim is a quotation that does not in any way deal with cost; it deals with improvements in AmerenUE's ability to restore service, i.e., the methods and practices used to restore service. The issue of how that improved ability impacts cost was not discussed. The portion of the record cited by MIEC reads as follows, with the question added for clarification:

Q. [from MIEC attorney Mr. Roam] OK. With those changes [addition of storm restoration trailers, mobile command centers, improvements to logistics and staging prior to a major storm], though, could I also turn that backwards and—and make the characterization that perhaps the storm

[217] Tr. p. 1586, l. 24 to p. 1587, l. 5.
[218] Tr. p. 1581, l. 24 to p. 1582, l. 14.
[219] MIEC's Initial Brief, p. 9.

recovery of 2006/2007 could have been a whole lot better if a number of these steps would have been taken prior to that time?

A. *Yeah. Yes, sir. I think—I think storm restoration could always get better, to be honest with you, and we learn from every one, and we do an after action meeting and look at what ways to improve, and we'll continue to do that as we move forward.*[220]

Further verifying that this discussion was not about cost, further examination of the questioning of Mr. Wakeman by Mr. Roam shows that the discussion centered around the scope and duration of outages rather than the cost of restoration:

Q. So if—if Ameren would have taken the steps between 2007 and 2009 prior to those storms of '06/'07, and I know this is getting complicated, do you think the size and duration of the outages would have been reduced, the scope and the duration of the outages would have been reduced?

A. *I'm not sure about the scope because I think the same damage would have occurred, but I think the duration might have been lessened, yes.*[221]

In fact, the driving factor for the cost of a storm restoration effort is the amount of damage done to AmerenUE's system by the storm, as Mr. Wakeman testified at the hearing: "The damage [from the storm] is the driving factor of the [restoration] cost of the storm and comes from the weather event as a direct—direct impact."[222] If the storm damage is the main driver of restoration costs and vegetation management efforts don't (and aren't designed to) reduce the scope of damage from a storm, then MIEC's assertion that restoration costs will go down in the future must be ignored.

Staff and MIEC argue that the better balance of the interests between AmerenUE and its customers is provided by the use of an AAO as compared to a tracker.[223] The Commission has already rejected this argument in relation to AmerenUE's request for a tracker in its last rate case. In that case, the Commission approved a request for a vegetation management and

[220] Tr. p. 1584, l. 4-13.
[221] Tr. p. 1584, l. 23 to p. 1585, l. 6.
[222] Tr. p. 1633, l. 16-18.
[223] Staff's Initial Brief, p. 59; MIEC's Initial Brief, p. 9.

infrastructure inspection tracker, saying that the tracker "…will ensure AmerenUE does not over-recover for its actual expenditures, as much as it ensures it does not under-recover those expenditures. Thus, the risk for ratepayers, as well as for AmerenUE, is reduced by operation of the tracking mechanism."[224]

Staff points out that a tracker will not improve AmerenUE's financial ratings[225] and MIEC points out that a tracker will not improve AmerenUE's storm restoration efforts.[226] The Company does not dispute either statement. However, the truth of those two statements does nothing to address the appropriateness of whether or not AmerenUE should be allowed to implement a tracker with the base level set at $10.4 million. The arguments supporting a tracker have been set forth multiple times – the Company does not control when a storm impacts its system yet is expected to restore service as soon as possible. The Company must make these expenditures yet has limited influence over the amount and no control over the timing of these expenditures. Given that none of these reasons have been disputed by any party in this case, there is ample justification for the Commission to approve the mechanism requested.

Finally, Staff points out that regulatory lag will occur with or without a tracker.[227] AmerenUE has never claimed that a tracker for these expenditures will eliminate regulatory lag, only that it will reduce excessive regulatory lag.[228] If the Commission were to authorize a tracker but not increase the amount included in the Company's revenue requirement, it would not reduce regulatory lag because AmerenUE would still be forced to recover expenditures through an AAO. The reduction to regulatory lag comes from the inclusion in AmerenUE's revenue requirement of a higher expense level. The tracker is the mechanism which protects both the

[224] Case No. ER-2009-0318, Report and Order, January 27, 2009, p. 41.
[225] Staff's Initial Brief, p. 60.
[226] MIEC's Initial Brief, p. 9.
[227] *Id.*
[228] AmerenUE's Initial Brief, p. 120.

Company and its customers from expenditure levels which are higher or lower than the amount included in the revenue requirement. It is the aspect which balances the interests of AmerenUE with those of its customers. The record contains ample justification for the Commission to include $10.4 million in the Company's revenue requirement and to authorize the Company to track the differences (whether above or below the base) through a tracking mechanism.

VII. MUNICIPALITIES.

The initial brief of the Municipal Group consisted of the repetition of the unsubstantiated allegations it made in its written testimony and at hearing. The Commission should note that AmerenUE's current street lighting rates were approved in AmerenUE's last rate case, where the Commission found them to be just and reasonable.

In the First Unanimous Stipulation and Agreement, which was approved by the Commission on March 24, 2010,[229] the Signatory Parties, including the Municipal Group, agreed that AmerenUE would complete a cost of service study for its streetlighting class and would work with the Municipal Group's consultant, the Staff and OPC in a collaborative fashion as part of that study. AmerenUE also agreed to develop a methodology to determine the value of systems and to negotiate with any 5M customer who wishes to purchase their streetlights. Finally, the agreement requires AmerenUE to develop a database to show the location of poles by type for each municipality.

AmerenUE believed that its agreement with the Municipal Group resolved all issues raised by the Municipal Group, although at the hearing, the Municipal Group continued to ask the Commission to place a moratorium on any increases for AmerenUE's streetlighting rates or, in the alternative, to require AmerenUE to hold in escrow any increase for this class pending the streetlighting study AmerenUE has already agreed to perform and, secondly, to eliminate future

[229] See *Order Approving First Stipulation And Agreement*, Case No. ER-2010-0036 (approved March 24, 2010).

pole installation charges from 5M customer bills until AmerenUE completes the streetlighting study discussed above.

AmerenUE does not believe any further relief has been justified by the Municipal Group's allegations and believes that at least a portion of the requested relief is not available to it under current Missouri law. Any change in the lighting class's relative share of revenues will be reviewed in AmerenUE's upcoming next rate case when there will be a comprehensive streetlight cost of service study available for the Commission's review. Indeed, that is the purpose of the study – to consider the study results and, if warranted, to change rates in the next rate case. Despite the *assertions* that the rates are incorrect, the Commission simply has no *evidence in this case* that AmerenUE's proposed rates for its streetlighting class are unjust or unreasonable.

The Municipal Group's proposal to escrow any rate increase, and make it "subject to refund," pending the results of the next rate case, is unreasonable and unlawful. The Municipal Group's proposal must be rejected as any refund based upon a rate design change in a future case would create a revenue shortfall that could not be recovered from other customer classes.[230]

AmerenUE also questions whether it is lawful for the Commission to impose interim rates "subject to refund" for only one class of customers under any circumstance without the agreement of the public utility, but it is undoubtedly unlawful to do so in the manner advocated by the Municipal Group. As the Company explained in its initial brief, this Commission has concluded in more than one case that it does not have the authority to order credits (refunds) but that the utility could agree to make the credits.[231] In this case, AmerenUE has not agreed to make any of its rates interim or to make them otherwise subject to refund.

[230] Tr. p. 2898, l. 20 to p. 2899, l. 4.
[231] AmerenUE's Initial Brief, pp. 141-142, citing *Report & Order, Staff v. Southwestern Bell Telephone Co.*, Case No. TC-93-224 & TO-93-192, 2 Mo.P.S.C.3d 479, 585 (December 17, 1993).

Finally, for a refund to be ordered in a subsequent rate case, there would have to be a finding that the lighting class rates resulting from AmerenUE's current rate case were not "just and reasonable." Such a finding and refund order would be the very definition of retroactive ratemaking. Under Missouri law, the Commission may consider past excess recovery insofar as it is relevant to the Commission's determination of what rate is necessary to provide a just and reasonable return *in the future* and avoid any *further* excess recovery.[232] However, the Commission cannot re-determine rates already established and paid without depriving the utility of its property without due process.[233]

The concerns raised by the Municipal Group are best resolved by allowing AmerenUE, working in concert with the Municipal Group's consultant, Staff and OPC, to complete the streetlight cost of service study and revisit this issue in the Company's next rate case. Until that time, there is insufficient evidence in the record to support the course of action requested by the Municipal Group.

VIII. FUEL ADJUSTMENT CLAUSE.

Other parties to this case have provided very little in the way of argument regarding the continuation of AmerenUE's fuel adjustment clause, subject to certain minor "housekeeping" adjustments supported by both the Staff and the Company. The Staff continues to support retention of the FAC in its current form, with a 95%/5% sharing. MIEC has recycled its previous proposal to subject AmerenUE to an 80%/20% sharing (subject to a cap of 50 basis points), but the only evidence MIEC provided was a re-submittal of Maurice Brubaker's 20-month old testimony from the last rate case, which the Commission rejected in that case. MIEC's Initial Brief devotes less than three full pages to the FAC issue, and attempts to make

[232] *See*, *State ex rel. General Tel. Co. v. Public Serv. Comm'n*, 537 S.W.2d 655 (Mo. App 1976).
[233] *See*, *State ex rel. UCCM v. Public Service Commission* 495 S.W.2d 45, 58 (Mo. 1979). *See also Lightfoot v. City of Springfield*, 236 S.W.2d 348, 353 (Mo. 1951); *Southwestern Bell Telephone Company v. Public Service Commission*, 645 S.W.2d 45 (Mo. App. 1979).

the point that the 5% sharing has less of an impact on AmerenUE than on Empire and KCPL-GMO, even though there is no current information about either of those companies in the record for this case. This argument is unsupported by evidence of record in this case, and in any event does not provide a justification for increasing the sharing percentage in AmerenUE's FAC.

In contrast to MIEC's almost non-existent support in the record in this case for its proposal, the Company has provided competent and substantial evidence of record that adoption of Mr. Brubaker's proposal would cost the Company tens of millions of dollars in prudently-incurred coal costs alone in just 2010 and 2011, and even more if higher nuclear fuel costs or lower off-system sales are taken into account.[234] Adoption of Mr. Brubaker's proposal would be tantamount to a disallowance of prudently-incurred costs in this rising cost environment, and would severely undermine one of the key provisions of S.B. 179, that is, that fuel adjustment clauses should be reasonably designed to provide the utility with a sufficient opportunity to earn a fair ROE.

Not only is greater sharing not needed, and not only would it be punitive, but Mr. Brubaker's dated analysis is flawed. The premise underlying Mr. Brubaker's analysis suggests that a hypothetical utility with large fuel costs, but that also has off-system sales that equal those large fuel costs, would face *no* uncertainty in its net fuel costs, when in fact it is undisputed that significant uncertainties exist both with respect to fuel costs and off-system sales revenues.[235] Moreover, actual experience has shown that Mr. Brubaker's analysis is flawed because it assumed (almost two years ago) net fuel cost uncertainty of just 35%, yet since the last case, the net fuel costs have swung about twice that amount, which would have created a far greater impact than Mr. Brubaker assumed.[236]

[234] Ex. 123, p. 13, fn. 5; p. 15, l. 11-16 (Barnes additional rebuttal).
[235] *Id.* p. 15, l. 4 to 21.
[236] *Id.* p. 15, l. 21 to p. 16, l. 4.

OPC spent a little more energy addressing the FAC in its initial brief, devoting just over four pages to the subject. However, the only evidence OPC provides is testimony by OPC witness Ryan Kind, who testified that it was his "belief" that the existing 5% sharing mechanism does not put enough of the Company's "skin in the game" to provide a proper incentive for the Company to act prudently in acquiring fuel and selling power in the off-system market. Mr. Kind's "belief" does not constitute competent and substantial evidence upon which the Commission could make a material change to AmerenUE's FAC, which would thereby subject the Company to a significantly increased risk of under-recovery of prudently-incurred fuel costs. In fact, none of the testimony provided by OPC or MIEC constitutes competent and substantial evidence that would support such a change.

In apparent recognition of this problem, OPC argues that as the moving party in this case AmerenUE has the burden of proof, that it is incumbent upon AmerenUE to prove that 95%/5% is the appropriate approach that will result in just and reasonable rates, and that the Company cannot meet this burden simply by pointing out that this approach has been used in the past.[237] In fact, AmerenUE has done far more than point out that this approach has been used in the past. AmerenUE has provided significant evidence of the need for and appropriateness of the existing FAC. To begin with, in its direct testimony, the Company submitted the extensive minimum filing requirements contained in the FAC rules and testimony from witness Lynn Barnes, including specific information addressing why the existing sharing mechanism is appropriate. Ms. Barnes explained why the FAC was needed in order for AmerenUE to have a sufficient

[237] OPC's Initial Brief, p. 17.

opportunity to earn a fair return on equity,[238] and why the standard criteria that the Commission has employed in determining whether to authorize an FAC continue to be met.[239]

Following the Commission's issuance of its order regarding the FAC issue, AmerenUE filed exhaustive additional testimony supporting the need for its FAC. This testimony addressed FAC issues involving policy, coal costs, nuclear fuel costs, natural gas costs, off-system sales revenues, modeling considerations and the impact on debt and equity cost and availability of materially changing the FAC.[240] AmerenUE's testimony showed how adversely its earnings would be impacted by a material change in the FAC (the Company's net fuel costs have increased by $118 million since just last year) and how the Commission has recognized that the vast majority of FACs across the country with which it competes for capital have no sharing mechanism in their FACs at all.[241] AmerenUE also provided testimony about the many incentives it has to operate its plants, procure fuel and make off-system sales prudently, including Commission prudence reviews and the very real risk it could lose the ability to use its FAC if it does not operate prudently. As Ms. Barnes testified, that risk alone is sufficient incentive to prudently manage the Company's net fuel costs.[242] The Company also provided evidence showing that it actually has acted in a prudent manner since its FAC was approved. For example, the equivalent availability of its plants has remained at very high levels and even increased since the FAC was approved.

None of the parties to this case challenged any of this testimony or even bothered to cross-examine many of the witnesses AmerenUE offered on the above-referenced subjects. The

[238] AmerenUE is already earning far less than its authorized ROE, even without requiring additional sharing under the FAC.
[239] Ex. 121, p. 7, l. 7 to p. 8, l. 7 (Barnes direct).
[240] Ex. 122 (Barnes additional direct); Ex. 123; Ex. 118 (Cannell FAC rebuttal); Ex. 132 (Finnell FAC rebuttal); Ex. 126 (Haro FAC rebuttal); Ex. 128 HC & NP (Irwin FAC rebuttal); Ex. 129 HC & NP Massmann FAC rebuttal); Ex. 124 (Neff FAC rebuttal); Ex. 120 (Rygh FAC rebuttal).
[241] *Id.*
[242] Ex. 123, p. 13, l. 14-19.

Company's evidence clearly shows that (a) the Company's fuel adjustment clause is needed to provide the Company with a sufficient opportunity to earn a fair return on equity, (b) the Company continues to meet the criteria the Commission has applied in determining whether to allow use of a fuel adjustment clause, (c) the Company has adequate incentives to act prudently in the operation of its system, the acquisition of fuel and the consummation of off-system sales, (d) the Company has actually acted prudently in these areas, and (e) increasing the sharing percentage in this rising cost environment would amount to a disallowance of prudently-incurred costs, which is inappropriate.[243]

In an attempt to argue that the 5% sharing in the existing FAC is insufficient to provide an adequate incentive to the Company, OPC compared that figure to the percentage of performance based pay various AmerenUE witnesses had. The percentages varied from 10% to 40%.[244] However, as AmerenUE pointed out at the hearing, net fuel cost is an *expense* that AmerenUE has no choice but to incur in order to serve its customers, and requiring AmerenUE to absorb a share of prudently-incurred fuel cost increases is much more analogous to requiring an employee to "share" a percentage of his or her travel expenses, a prudently-incurred cost in the service of his or her employer that the employee has to incur, in order to incentivize them to stay at reasonably priced hotels and buy gas at reasonably priced gas stations. Although most employers don't require their employees to "share" any of the prudent expenses they incur, requiring them to share 20% of those expenses is clearly unreasonable, is unnecessary to ensure prudent behavior, and is punitive.

[243] Because net fuel costs are calculated using a multi-year average of power prices, and because power prices have declined sharply in recent months, AmerenUE's off-system sales revenues built into its net base fuel costs are already overstated. As a consequence, AmerenUE will immediately lose money if its sharing percentage is increased.
[244] OPC's Initial Brief, p. 17.

For all these reasons, the Commission should retain AmerenUE's FAC in its present form, with the housekeeping modifications agreed to by the Company and Staff, together with the modifications agreed upon in previous stipulations filed in this case, which have already been approved by the Commission.

Dated: April 30, 2010

Respectfully submitted:

SMITH LEWIS, LLP

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