Schedule No.:	
Issues:	**Merger Savings/Merger Costs/ Merger Premium/Ratemaking Treatment/Utility Operations**
Witness:	**Gary L. Rainwater**
Type of Schedule:	**Direct Testimony**
Sponsoring Party:	**Union Electric Co.**
Case No.:	

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. EM-96-149

DIRECT TESTIMONY

OF

GARY L. RAINWATER

St. Louis, Missouri
November 2, 1995

MISSOURI PUBLIC SERVICE COMMISSION

STATE OF MISSOURI

In the matter of the Application of Union Electric Company for an order authorizing: (1) certain merger transactions involving Union Electric Company; (2) the transfer of certain Assets, Real Estate, Leased Property, Easements and Contractual Agreements to Central Illinois Public Service Company; and (3) in connection therewith, certain other related transactions.	)	Case No.________________

AFFIDAVIT OF GARY L. RAINWATER

State of Missouri)
) SS.
City of St. Louis)

Gary L. Rainwater, being first duly sworn on his oath, states:

1. My name is Gary L. Rainwater. I work in the City of St. Louis, Missouri, and I am the Vice President of Corporate Planning at Union Electric Company.

2. Attached hereto and made a part hereof for all purposes is my Direct Testimony consisting of pages 1 through 29, inclusive, all of which testimony has been prepared in written form for introduction into evidence in the above-referenced docket.

3. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded are true and correct.

GL Rainwater

Gary L. Rainwater

Subscribed and sworn to before me this 2nd day of November 1995.

GL Waters

Notary Public

G. L. WATERS
Notary Public — Notary Seal
STATE OF MISSOURI
St. Louis County
My Commission Expires: March 16, 1999

DIRECT TESTIMONY

OF

GARY L. RAINWATER

MISSOURI PUBLIC SERVICE COMMISSION

Background

Q. Please state your name and business address for the record.

A. My name is Gary L. Rainwater and my business address is 1901 Chouteau, St. Louis, Missouri, 63103.

Q. By whom are you currently employed and in what position?

A. I am employed by Union Electric Company (UE) as Vice President of Corporate Planning.

Q. Please describe your educational background.

A. I have a Bachelor of Science Degree in Electrical Engineering from the University of Missouri at Columbia and a Master of Science Degree in Systems Management from the University of Southern California.

Q. Would you please review your work experience?

A. I have been employed by UE since September 1979, working first in Transmission and Distribution, then moving into Corporate Planning in September 1982. I was promoted to General Manager of Corporate Planning in July 1988 and to Vice President of Corporate Planning in July 1993.

Q. What are your responsibilities as Vice President of Corporate Planning?

A. They include sales and peak demand forecasting, integrated resource planning, transmission planning, rate design, bulk power marketing, and natural gas supply and planning. I also chair Union Electric's Planning Coordinating Committee, which is a group of officers responsible for developing our company's five-year business plan.

Union Electric Operations

Q. Please describe the business operations of Union Electric.

A. Union Electric is a Missouri corporation, also authorized to do business in Illinois.

The principal business of Union Electric is to provide electric energy to customers in a 24,000 square-mile area of Missouri and Illinois. Our Missouri service area includes the City of St. Louis and St. Louis County, and all or portions of 65 other counties. Our Illinois service area includes the cities of East St. Louis and Alton. In addition to the retail electric business, UE serves 16 wholesale electric customers, all of which are located in Missouri.

Another business of Union Electric is to provide natural gas service to customers in 22 Missouri counties and two Illinois counties. Our company also provides steam service in Jefferson City, Missouri.

Q. Approximately how many customers are served by Union Electric Company?

A. As of December 31, 1994, we provided retail electric service to approximately 1,060,000 customers in the state of Missouri and 64,000 in the state of Illinois. In addition, we provide wholesale electric service to the 16 customers I mentioned earlier. We provide natural gas service to approximately 100,000 customers in Missouri and 18,000 customers in Illinois.

Q. How many employees does Union Electric have?

A. As of December 31, 1994, UE had 6,266 employees in its two-state operations.

Q. Does Union Electric have any business interests other than those described above?

A. Yes, there are two other interests which are held by UE and operated through subsidiary corporations. UE is the sole owner of Union Electric Development Corporation, formerly known as Union Colliery, and UE is a 40 percent owner of Electric Energy, Inc.

Q. Would you please describe the operations of Union Electric Development Corporation?

A. Yes. Union Electric Development Corporation (UEDC) was originally organized as Union Colliery Company, but was recently renamed Union Electric Development Corporation. UEDC is used to own civic related projects within our service area.

Q. Would you please describe the operations of Electric Energy, Inc. (EEI)?

A. Yes. EEI is a company that was formed in the early 1950s to provide electric energy to a uranium enrichment plant located near Paducah, Kentucky. The enrichment plant was originally operated by the Atomic Energy Commission and is operated today by the United States Enrichment Corporation. EEI owns the Joppa Plant, a 1,015 MW coal-fired power plant located near Joppa, Illinois, and six 161 kV transmission lines which transmit power from the Joppa Plant to the Paducah enrichment plant.

EEI's common stock is held by four utility companies. In addition to UE's 40 percent ownership, Illinois Power owns 20 percent, Kentucky Utilities owns 20 percent, and Central Illinois Public Service Company (CIPS) owns 20 percent.

Q. How are UE's business operations regulated?

A. Our retail electric, natural gas and steam operations in Missouri are regulated by the Missouri Public Service Commission. Our electric and natural gas operations in Illinois are regulated by the Illinois Commerce Commission. Our wholesale electric sales are regulated by the Federal Energy Regulatory Commission, as are the electric sales of EEI.

Q. Is UE also regulated by the Securities and Exchange Commission for purposes of compliance with the Public Utility Holding Company Act (PUHCA)?

A. While UE is technically a holding company, UE has received an exemption from most of the requirements of PUHCA.

CIPSCO Operations

Q. Please describe the business operations of CIPSCO.

A. CIPSCO was incorporated in 1986 and became the parent holding company of CIPS, its utility operating subsidiary, in 1990. CIPSCO, through its CIPS subsidiary, supplies electricity and natural gas services in a 20,000 square-mile region of central and southern Illinois.

CIPS was organized in 1902 and now serves 317,000 retail electricity customers in 557 communities. It also distributes natural gas to nearly 166,000 customers in 267 communities. CIPS' service territory has an estimated population of 820,000 and covers about 35 percent of Illinois.

CIPSCO conducts its non-utility businesses through a second subsidiary, CIPSCO Investment Company. CIPSCO Investment manages CIPSCO's non-utility investments, including leveraged leases, marketable securities and energy projects.

Q. How many employees does CIPSCO have?

A. As of December 31, 1994, CIPSCO had 2,669 employees.

Purpose of Testimony

Q. Are you familiar with Union Electric's application to combine its business with CIPSCO, Incorporated?

A. Yes. I was involved in the negotiation phase of the proposed merger, primarily in estimating merger-related cost savings. Since the merger was announced, my work has focused on planning for the integration of the combined companies' operations.

Q. What is the purpose of your testimony in this case?

A. I will provide an overview of the proposed transaction, discussing the issues we believe are relevant to a Commission decision to approve the combination of Union Electric and CIPSCO. I will summarize the transaction's economic benefits, discuss cost-of-service issues, and describe how we expect cost reductions to accrue to UE and CIPS as a result of the merger. I will also propose a method for treating transaction costs for ratemaking purposes, and I will discuss operational impacts of the merger.

Overview of Transaction

Q. Please describe the proposed transaction between UE and CIPSCO.

A. Union Electric and CIPSCO have agreed to combine their businesses through the creation of a new holding company, Ameren Corporation, which will own both UE and CIPS as separate utility operating companies. The "Agreement and Plan of Merger" is attached as my Schedule 1 and explains in detail how this combination will be accomplished.

Mr. Charles W. Mueller also describes the merger in his testimony and includes a Schedule 2 which depicts the surviving corporate structure. That schedule provides an easy way to understand key elements of the combination. Note that both UE and CIPS will survive as separate corporate entities under Ameren.

Q. Will Ameren Corporation register as a holding company?

A. Yes. Ameren will be a registered holding company under the Public Utility Holding Company Act of 1935. As such, Ameren and its subsidiaries will need SEC approval to issue securities, acquire the stock of another public utility, amend its articles of incorporation or acquire stock, extend credit, pay dividends, lend money or invest in another business

Q. Will UE and CIPS be changed in any way by the merger?

A. Yes. As part of the merger, UE will transfer its Illinois retail electric and gas business and related facilities to CIPS, making CIPS the exclusive Illinois operating branch of the combined companies. That will leave UE with retail utility business operations only in Missouri, although UE will retain its electric transmission and generation facilities located in Illinois.

Q. Why is that property transfer being proposed?

A. To simplify regulation of the operating companies. Without the proposed property transfer, UE would remain both a Missouri and an Illinois utility subject to all rate and other regulatory filing requirements of both the Missouri Public Service Commission and the Illinois Commerce Commission. With the transfer, most Illinois regulatory requirements will be eliminated for UE; and, since CIPS is already an Illinois utility, the transfer should impose few or no additional regulatory requirements on CIPS.

Q. How will the management of the new holding company structure function?

A. Charles W. Mueller will become Chairman of Ameren Corporation and will remain President and CEO of UE. Clifford L. Greenwalt will become Vice Chairman of Ameren and will remain President and CEO of CIPS.

In addition, a Board of Directors will be formed for Ameren which will be composed of ten board members to be named by UE and five board members to be named by CIPSCO. UE's board will be expanded by one, with the addition of Mr. Greenwalt. CIPS' board will be expanded by three, with the addition of Mr. Mueller and two other members to be named by UE.

Beyond those changes, no final decisions to change management structure have been made.

Q. Is the need for additional management or structural changes being considered?

A. Yes. We recognize that some changes will need to be made in order to achieve the planned economies of operations. To address this issue and many more detailed questions related to the merger, we have formed a Transition Management Task Force. The Task Force is made up of eighteen transition teams, each assigned to address specific aspects of the merger. We expect to complete this transition planning work by March, 1996. Organization of the Transition Management Task Force is shown in my Schedule 2.

Q. Would you please describe the rationale for this business combination?

A. Yes, our rationale is simple. Our purpose is to reduce the combined operating costs of UE and CIPS.

Cost reduction has been a key element in UE's business strategy for the past ten years. As a result of aggressive cost reductions, our Callaway rate phase-in plan was terminated in 1987, thereby avoiding scheduled electric rate increases totaling \$189 million that would have occurred in 1988, 1989, and 1990. Through continued cost reductions, our electric rates have been reduced by an additional \$100 million: by

$30 million per year in 1990, $40 million per year in 1993, and another $30 million per year in 1995.

Unfortunately, cost reduction is a strategy that has practical limits, and our company is approaching those limits. Without some fundamental change in the way we do business, it will become increasingly difficult to continue reducing costs. Combining our utility operations with CIPS offers an opportunity to achieve more cost efficiency than either company can achieve independently.

Q. Why are continued cost reductions so important to UE?

A. For three reasons.

First, we have a basic obligation to our customers to operate as efficiently as possible.

Second, we also have an obligation to provide a fair return to our shareholders, and cost reduction has been a key element in our ability to do so. The Commission, of course, has also played a role in this regard. The Commission's willingness to allow investors and customers to share in cost reductions, through rate moratoriums and incentive regulation, has provided us a continuing incentive to cut costs.

Finally, the electric utility industry may become more competitive and may eventually be deregulated. While direct retail competition and deregulation may or may not be in the public interest, and while it may or may not occur in Missouri, we cannot ignore that possibility. Cost reduction is our most effective way to prepare for competition, since lower costs mean lower rates.

Q. Has UE's customer service suffered due to cost reductions?

A. No. In fact, our customer service has steadily improved, as indicated by our customers' opinion of our performance. UE's Customer Satisfaction Index (CSI) has improved from an index of 69.8 five years ago, to 75.0 today. The CSI is not a percentage. It is a relative measurement that allows us to track customer satisfaction over time.

Cost of Service Impacts of Merger

Q. To what extent does UE expect to reduce costs by combining with CIPSCO?

A. We expect to reduce UE's and CIPSCO's combined costs by approximately $590 million over a ten-year period. Schedule 3 to this testimony shows our estimated savings on a year-by-year basis for a ten-year period. By the tenth year, cost reductions will reach a level of about $80 million per year.

Q. Is that a reasonable estimate?

A. Yes. I would characterize it as both reasonable and achievable.

Q. What gives you that confidence?

A. We employed Deloitte & Touche Consulting Group, a division of Deloitte & Touche LLP, to assist in our merger study and to verify our results based on their knowledge of other mergers. Deloitte & Touche has developed an extensive data base to perform such studies and is recognized within the industry as the foremost merger synergy expert. Mr. Thomas Flaherty of Deloitte & Touche will explain the analysis his firm performed jointly with UE and CIPS, and will testify to the reasonableness of the results. Additionally, Ms. Maureen Borkowski will testify to certain aspects of these savings.

Beyond Mr. Flaherty's and Ms. Borkowski's judgments, however, I have confidence in our own record of cost reduction. Union Electric's track record in this regard is among the best in the industry. It is our intent to manage the merger transition to ensure that these savings will be achieved. We are confident that we will do so.

Q. In what areas do you expect to achieve these cost savings?

A. Again, I will refer you to my Schedule 3. That schedule breaks down savings into five categories, as follows:

- $204 million in administrative and general expenses
- $196 million in staffing reductions
- $84 million in electric production savings
- $69 million in purchasing economies
- $37 million in natural gas economies

The administrative category includes savings due to combining customer information systems, combining call center systems, and combining automated mapping and facilities management systems. It also includes other items such as combining insurance programs, benefits programs, and stockholder service programs.

Staffing savings are based on reducing UE's and CIPS' joint staffing by 295 positions over the ten-year period. These staff reductions will be predominantly in the administrative areas of the companies, which we expect to combine in some form over a period of several years. We hope to make these reductions essentially through attrition, just as UE has already made approximately 1,300 staff reductions over the last ten years through attrition.

Electric production expenses, which are primarily fuel expenses, will be reduced by jointly dispatching UE's and CIPS' power systems and coordinating plant maintenance schedules.

Non-fuel purchasing savings will be achieved by increased efficiency in purchasing materials and supplies, and by centralizing purchasing and inventory functions.

Natural gas costs will be reduced through increased purchasing efficiency.

Mr. Flaherty and Ms. Borkowski will explain these savings in more detail in their testimony and Schedules.

Q. Referring again to the proposed transfer of UE's Illinois distribution and customer service facilities to CIPS, would you please describe the facilities that would be affected?

A. Schedule 4 of my testimony identifies the specific facilities which will be transferred to CIPS. It includes all of our electric and gas facilities used to provide retail service in Illinois. It does not include any generation or transmission facilities.

Q. Will the transfer of those facilities have any impact on electric or natural gas distribution costs charged to Missouri customers?

A. No. Currently, the cost of owning and operating those facilities is assigned directly to UE's Illinois customers. After the transfer, those costs will be assigned to CIPS' Illinois customers, leaving Missouri customers unaffected.

Q. Will the transfer of UE's Illinois customers to CIPS have an impact

on the allocation of power costs to Missouri customers?

A. It will have no material impact because we have structured the transaction to minimize power cost reallocations.

Currently, UE provides approximately 500 MW of firm power and 70 MW of interruptible power to serve our Illinois customers. Following the merger, UE will continue to provide that same amount of power to CIPS through a System Support Agreement. The price of that power will be set to recover, as closely as possible, the same amount of our power costs that we would have formerly recovered through Illinois retail sales. That will leave Missouri customers virtually unaffected by this aspect of the merger.

Q. Has the System Support Agreement been developed?

A. Yes. It is sponsored by Maureen A. Borkowski as part of her testimony.

Q. The need for the System Support Agreement seems to be related to your decision to structure the merger under a holding company, with operating companies aligned along state lines. Is that true?

A. Yes. Merging UE and CIPS would have avoided the need for the System Support Agreement, since that would have merged the entire generation and transmission rate bases of both companies. However, that approach might have caused cost reallocations between Missouri and Illinois due to differences between UE's and CIPS' generating capacity costs, fuel costs and generation reserve margins. We have used the operating company structure, combined with the System Support Agreement, to avoid those problems. Our intent was to ensure that neither state would be harmed by the merger. We have accomplished that by preserving, as closely as possible, the existing power cost allocations in both states.

Q. Are there any other factors related to the transfer of Illinois facilities or customers which could impact Missouri customers' cost of service?

A. Yes. We also allocate a portion of our company's overall administrative and general (A & G) costs to our Illinois jurisdiction. However, since UE will no longer have an Illinois jurisdiction following the merger, this raises the question of what will happen to those costs.

Q. What will happen to those costs?

A. A portion of those costs, the amount attributable to power supply, has been included in the System Support Agreement.

As for the remainder of those costs, the ultimate allocation depends on organizational and service issues that are now being analyzed by our Transition Task Force. However, I do not expect the level of A & G support that UE currently provides to its Illinois service area to change significantly following the merger. Therefore, I do not expect the overall allocation of UE's A & G costs attributable to our Illinois jurisdiction to change significantly following the merger. UE will, however, require a contractual method of charging those costs to CIPS, since our Illinois service area will become part of the CIPS system.

Q. Have you developed a contract for that purpose?

A. Yes. We have developed a General Services Agreement which is attached as Schedule 5 to my testimony. That agreement sets out the basic principles under which one affiliate will charge for services provided to one or more other affiliates. In the specific case of our Illinois administrative cost allocation, we would use this agreement to continue that allocation, as long as UE continues to provide the same level of administrative service.

Q. Isn't there also a broader cost allocation issue regarding how the cost of services provided jointly, for both operating companies, will be divided between the operating companies?

A. Yes. We expect to organize the administrative functions of both UE and CIPS so that they operate as a joint service organization. This will be essential in order to achieve the planned merger savings. There are still questions regarding how these functions will ultimately be organized; either within UE, within CIPS, or within a joint service company. The General Services Agreement, therefore, has been written with enough flexibility to allow for any ultimate organizational structure.

Q. How will you achieve a correct allocation of administrative or service costs between the operating companies?

A. We will accomplish that through conventional accounting practices and allocation methods. Assuming that services are provided by UE for CIPS, we will charge an allocated share of UE's costs to CIPS pursuant to the principles of the General Services Agreement. Any CIPS services performed for UE would be allocated and charged to UE pursuant to the same principles. A similar procedure would be used if services were provided by a service company. Warner L. Baxter, our accounting witness, addresses these cost allocation issues in his testimony.

Q. Have you considered how merger-related cost reductions will be shared between the UE and CIPS operating companies?

A. Yes. Overall, we expect that merger savings will flow to UE and CIPS in proportion to the size of the electric and natural gas businesses in each company. About 70 percent of electric savings will flow to UE and 30 percent will flow to CIPS. In natural gas, we expect the split to be about 30 percent to UE and 70 percent to CIPS.

Q. What is your basis for those conclusions?

A. Answering that question requires explaining each of the savings components individually. Consider administrative savings first.

Combining the UE and CIPS administrative functions, pooling A & G costs, and then allocating those costs through conventional allocation methods, would result in allocation of approximately 70 percent of the combined systems' A & G costs to UE and 30 percent to CIPS. Therefore, as combined costs are reduced, the reductions will flow in those same proportions.

Labor savings should flow in approximately the same proportions as A & G savings. That will happen because labor savings will result from combining service functions of the two companies, pooling those costs, and then allocating the reduced costs between UE and CIPS. Therefore, both labor costs and labor savings will flow to CIPS and UE through the method used to allocate shared costs. Again, that will result in approximately 70 percent of savings going to UE and 30 percent going to CIPS.

Joint dispatch savings should flow approximately in proportion to the electric sales of each company, which also should result in 70 percent going to UE and 30 percent going to CIPS.

Purchasing economies should accrue in proportion to the purchasing volumes of the companies or in proportion to the A & G allocation between the companies, depending on types of materials purchased. Both of those ratios indicate that about 70 percent of savings would flow to UE and 30 percent to CIPS.

And finally, the reduction in natural gas costs will be passed through to Missouri and Illinois customers through the purchased gas cost adjustment ("PGA") provisions of CIPS and UE tariffs. The exact method of calculating PGA cost components will depend upon several factors, including each company's load and demand on a particular pipeline, and the nature of the applicable gas contracts. Generally, UE has approximately 30 percent of the gas load by volume, while CIPS has 70 percent. Reductions in purchased gas costs should therefore occur in approximately those proportions.

Proposed Ratemaking Treatment

Q. Turning now to ratemaking treatment, do you propose that merger-related savings begin flowing through to your customers immediately following the merger?

A. Yes, in part. We also propose, however, that our stockholders be allowed an opportunity to recover the investment which was required to achieve those savings, and be allowed to share in net merger savings.

Q. Why is that appropriate?

A. Because Ameren Corporation's shareholders will incur a merger premium of $232 million and will incur other transaction costs of $41 million in order to complete the merger. That represents a $273 million investment which will return

$590 million in savings over a ten-year period, an additional $970 million in the second ten-year period, and almost $1.4 billion in the third ten-year period. However, unless this investment is recognized in our rates, shareholders will have little chance to recover their costs and no chance to earn a return on that investment.

This proposal to recover our merger investment is conceptually no different from any utility proposal to recover an investment that achieves savings in operating costs. The merger represents an investment in business structure to achieve a structural efficiency improvement. Its recovery should be allowed for the same reasons that an investment in any aspect of our business would be allowed—because it was prudent.

Q. Do you consider your investment in this merger to be prudent?

A. Yes. The merger will reduce the combined companies' costs by over $2.9 billion over a 30-year period. Even if our customers paid the entire $273 million immediately after closing, their expected cost savings would represent more than a 20 percent return on investment. This would be considered prudent by any reasonable standard.

Q. What is the basis for the $273 million merger investment?

A. As explained previously, there are two components of this investment. One is a $232 million merger premium, which is based on the effective cost above market that Ameren Corporation will pay to acquire the stock of CIPSCO. Calculation of that amount is shown in my Schedule 6. The other is made up of various transaction-related charges totaling approximately $41 million. Tabulation of those charges is shown in my Schedule 7.

Mr. Douglas Kimmelman of Goldman Sachs will discuss in his testimony additional reasons why Ameren's shareholders should be allowed to recover the $232 million merger premium.

Q. How do you propose to recover Ameren's investment?

A. Through a shared savings plan, a plan which will allow stockholders and customers to share equally in the net merger savings.

Q. How will the shared savings plan work?

A. It will allow stockholders to recover their direct merger investment, the $273 million I've referred to, over a ten-year period. The plan will amortize that investment in proportion to expected savings in each of the ten years, to ensure there are net savings in each year. It will then split the net savings equally between shareholders and customers.

Q. Would you please describe in more detail how that plan will operate, on a year-by-year basis?

A. Yes. Please refer to my Schedule 8, the Shared Savings Plan.

This schedule shows, on a year-by-year basis, how our merger investment will be amortized, how a portion of projected net savings will be allocated to cost of service, and how an equal portion of net savings will be made available to reduce customers' cost of service.

For example, consider the year 2000, the fourth year following the merger assuming it is completed at the end of 1996. We expect that the merger will reduce UE's and CIPS' combined costs in that year by $52.8 million. That is 8.96 percent of the $590 million of total savings over ten years, so we would charge 8.96 percent, or $24.5 million, of our merger investment as a pro-forma cost of service in that year.

That leaves approximately $28 million in net savings, which would be split equally between stockholders and customers, i.e., $14 million would be charged as a pro-forma adjustment to UE's and CIPS' costs of service and $14 million would be made available to benefit customers.

Q. Would your proposed method of sharing net savings allow your stockholders to recover more than their investment in the merger?

A. No. Recovering our full investment would require recovering the full $273 million direct investment plus a return to account for the time value of money. The present value of our proposal, calculated at a 9.52 percent discount rate, is only $254 million. Consequently, this proposal will actually provide stockholders $19 million less than full recovery of their investment.

Q. What is the basis for using a 9.52 percent discount rate in the present value calculation?

A. That is the discount rate we currently use for long-term planning purposes. It is based on our estimates of long-term debt and equity costs.

Q. Why are you proposing to recover less than your full investment?

A. Because our proposal is inherently fair and equitable in the sense that it shares net savings equally between stockholders and customers. Although it is somewhat short of full cost recovery, continuing incentive regulation offers the possibility of making up any earnings shortfall by beating our merger savings estimates. That will provide a powerful performance incentive to company management. We would hope that when UE's current incentive rate agreement expires in 1998, we will be able to simply extend that agreement, thereby extending the performance incentive and continuing to flow merger-related savings to customers.

Q. Do you propose to recover your entire merger investment, including one-half of the net merger savings, in UE's retail electric jurisdiction?

A. No. We propose to divide the investment into six jurisdictional components in proportion to how we expect the merger savings to accrue to each of those jurisdictions. The percentage allocations are as follows:

Jurisdiction	Investment Allocation
UE Retail Electric	58.7%
UE Wholesale Electric	3.5%
UE Gas	3.6%
CIPS Retail Electric	22.5%
CIPS Wholesale Electric	3.9%
CIPS Gas	7.8%
TOTAL	100.0%

Q. How did you determine those percentage allocations?

A. They were determined based on our assessment of how the merger savings will flow to each of those jurisdictions. As I explained earlier, we expect savings to flow to Ameren's Missouri and Illinois electric and gas businesses essentially in proportion to the size of those businesses. For the staffing, A & G and purchasing savings, we've used a composite allocation method to estimate how savings will flow.

The composite allocator is based on an average of labor, sales, peak demand and customer ratios derived from 1994 FERC Form 1 data. For the joint dispatch and natural gas purchasing categories, we've divided savings based on the amounts of electricity and natural gas sold in each jurisdiction. We then calculated the total savings in each jurisdiction and divided the merger investment proportionately. Schedule 9 to this testimony shows the calculation of jurisdictional allocation factors, and Schedule 10 details the pro-forma jurisdictional cost of service allocations required to recover Ameren's merger investment in each of six jurisdictions.

Q. Why have you allocated merger cost recovery in proportion to merger savings?

A. Because the purpose of the merger is to reduce costs. It is an investment in cost reduction. Therefore, the investment should be allocated in proportion to cost reductions.

Q. Do you plan to seek recovery of the amounts of your merger investment indicated in your Schedule 10 in each of those jurisdictions?

A. Yes. We plan to propose the same shared savings approach for cost recovery in each jurisdiction.

Q. Are you proposing an electric rate increase to recover the amortized costs of your merger investment?

A. No. We are simply asking that the Commission approve recovery of our investment based on the shared savings plan we have proposed. We would hope to recover the amortized merger costs over the next ten years without the need for a rate increase. The cost reductions created by the merger will help to achieve that objective.

Q. Please explain why you have proposed amortizing the merger investment in proportion to savings over the ten-year period.

A. We proposed this method to ensure that savings will exceed the amortized costs in every year, and to ensure that the merger will have no detrimental impact on rates in any year.

Using this method, the expected merger savings in the first ten years following the merger will exceed the amortized merger investment by approximately 37 percent. That will provide the Commission reasonable assurance that net savings will be available to benefit customers in every year following the merger.

Q. Would you please explain that last point -- what do you mean by reasonable assurance?

A. A concern the Commission may have in approving our shared savings plan is that actual merger-related savings may not equal or exceed the pro-forma charges to cost of service that we have proposed in Schedule 10. The Commission needs reasonable assurance that this will in fact occur. The fact that expected merger savings exceed our proposed cost recovery by a wide margin, approximately 37 percent in every year, provides that reasonable assurance. Further assurance is provided by our company's track record in achieving cost reductions on its own. We intend to meet these cost reduction projections for the reasons I outlined earlier:

- To reduce our customers' costs through improved efficiency,
- To improve our shareholders' return through incentive regulation, and
- To prepare both UE and CIPS for possible deregulation.

Q. Wouldn't it provide even more assurance if the Commission conditioned recovery of your merger investment on a detailed documentation of actual savings?

A. It would if that were possible. Unfortunately, that kind of detailed documentation is not possible.

Tracking and documenting merger savings would require comparing actual costs against hypothetical costs, costs which would have occurred without the merger, but did not occur because the merger eliminated them. Those hypothetical costs are inherently unknowable, and attempting to track them for ten years following the merger would be literally an impossible task.

A Commission imposed tracking requirement would only lead to prolonged second guessing and debate about hypothetical costs, and would burden both the Commission and Company for an extended period. A far more reasonable approach is to allow recovery of these costs based on the prudence of the investment and a reasonable estimate of benefit to customers.

Q. Can you provide any other reasonable assurance that customers will benefit from the merger by an amount in excess of costs to recover your merger investment?

A. Yes. We are proposing to recover our merger investment over ten years. The merger benefits will continue indefinitely, and beyond ten years our customers' cost of service will be reduced by 100 percent of those benefits. Ultimately, customers will receive billions of dollars of merger-related savings. We are asking only to recover the investment which was necessary to achieve those savings.

Q. How do you propose treating merger cost recovery during the remaining term of UE's 1995 electric incentive rate agreement?

A. The amortized portion of our merger costs, including one-half of net savings as shown in Schedule 10, should be accounted for above the line as an adjustment to cost of service. There is no reason to treat a merger investment any differently than any other prudent investment, and doing so would be equivalent to a disallowance. The incentive agreement will still provide the proper incentive for management to operate as efficiently as possible, and will still return the proper rate credits to customers if and when that is appropriate. The chances of that plan actually returning credits to customers will be improved after the merger, due to savings which would not have occurred without the merger.

Mr. Baxter addresses these issues in more detail in his testimony.

Q. If your incentive rate agreement were extended beyond July, 1998, how would you propose treating merger cost recovery during the extension period?

A. Above the line, exactly as I have proposed for those costs to be treated during the current agreement. There would be no reason to alter the recovery schedule.

Q. When that agreement ultimately expires, how do you propose treating merger cost recovery?

A. Above the line, exactly as I have proposed above. In any rate case test year, the amount shown in Schedule 10 would be used as an addition to the cost of service in setting rates. Again, there would be no reason to alter the cost recovery schedule and doing so would be equivalent to disallowing the investment which was necessary to create the merger savings.

Operational and Customer Service Issues

Q. Turning now to operational and customer service issues, will the proposed merger have any impact on service in the UE area?

A. Following the merger, UE will provide retail service in Missouri only. CIPS will provide retail service in Illinois only. Since the Missouri side of our business will be essentially unchanged due to the merger, service in Missouri will be essentially unaffected by the merger, with one possible exception. There is a possibility that the merger will improve our customer call response times, particularly during storms. We would achieve that improvement by integrating UE's call center operations with CIPS' call center operations, which are now under development. That would provide either center the capability of backing up the other, which should improve service during the high call volume periods we experience due to storms.

Q. Would the economy in your service area be impacted?

A. Yes, to the extent that lower electric rates attract more industry and produce greater job growth, the economy of our service area will benefit from the merger.

Q. What about environmental programs—would UE's be impacted in any way?

A. We will likely manage UE's and CIPS' environmental programs jointly, resulting in some cost savings. However, our diligence in complying with environmental laws and regulations will not be affected in any way.

Q. Is it possible that the merger might affect UE's community involvement?

A. Only in a positive way. We have always been primarily a Missouri company, but with a small Illinois business. With the merger, UE will be solely a Missouri company, focused solely on its Missouri communities. CIPS will have a parallel role in Illinois. We expect that this division of responsibility and corporate identity will have a positive impact on community involvement and service in both states.

Q. Could the reliability of your power supply system be impacted in any way?

A. There should be no material change in power supply system reliability due to the merger, although there could be some small improvement due to improved maintenance coordination between UE and CIPS.

Q. From a regulatory point of view, would UE's relationship with the Missouri Commission be changed in any way by the merger?

A. Only in the sense that UE's retail business will now fall under the sole jurisdiction of the Missouri Commission, rather than being split between the Missouri and Illinois Commissions. This seems to us a much more logical way to organize our business. Conflicting requirements of the MPSC and the ICC have in the past presented problems in areas such as resource planning and fuel purchasing. With the UE and CIPS operating companies organized along state lines, regulatory responsibility and authority will become more sharply defined.

Q. Will UE become a registered holding company following the merger?

A. Following the reorganization, Ameren Corporation will become a registered utility holding company under PUHCA. We do not expect that to be a problem. The main difficulties utilities have experienced as registered holding companies are the PUHCA limitations on diversification into non-utility businesses. Union Electric's primary business interest is not in diversification. We are a company focused on our regional, Missouri and Illinois, utility business. The merger will in no way change that focus or change our business philosophy.

Our primary reasons for adopting a registered company structure are those I have already discussed. The separation of operating companies clarifies state commission authority and prevents mixing of generation rate bases which might have caused an adverse effect in one state or the other. Our only other reason for choosing a registered structure was CIPS' strong desire to maintain its corporate identity in Illinois, which we agreed was a sound business strategy in Illinois. Focusing UE's identity in Missouri is also sound business strategy.

Q. What effect, if any, will Ameren's registration as a holding company under PUHCA have on state regulation?

A. Even though Ameren will be a registered holding company under PUHCA and subject to the jurisdiction of the Securities and Exchange Commission, UE will remain a public utility subject to the Missouri Commission's jurisdiction over matters relevant to the provision of gas and electric service to customers in Missouri. Additionally, the Missouri Commission will have the same access to the books and records necessary to regulate public utility service that it now has.

On a related matter, we note that the SEC could require, as a condition for approval of the Merger, that UE and CIPS divest their gas utility properties, and possibly certain non-utility investments of UE and CIPSCO. We do not believe this is likely based on other transactions that have been approved by the SEC.

Conclusion

Q. Is it your conclusion, then, that the combination of Union Electric and CIPSCO is in the public interest?

A. Yes.

We have carefully structured our merger to avoid the possibility of any detrimental impact, and we expect to achieve significant economies and operational benefits. In coming decades, this combination will save our Missouri customers billions of dollars. In our view, the proposed combination of Union Electric and CIPSCO serves the public interest both in Missouri and in Illinois.

Q. Does that conclude your direct testimony?

A. Yes, it does.

G. L. Rainwater Testimony

Summary of Schedules

Schedule 1	-	Agreement and Plan of Merger
Schedule 2	-	Transition Management Task Force
Schedule 3	-	Summary of Merger Savings
Schedule 4	-	Illinois Facilities to be Transferred
Schedule 5	-	General Services Agreement
Schedule 6	-	Calculation of Merger Premium
Schedule 7	-	Pre- and Post-Merger Transaction Costs
Schedule 8	-	Shared Savings Plan
Schedule 9	-	Calculation of Jurisdictional Allocation Factors
Schedule 10	-	Pro-forma Jurisdictional Cost-of-Service Allocations