

Exhibit No.:

Issue(s): Environmental Cost Recovery Mechanism

Witness/Type of Exhibit: Trippensee/Direct

Sponsoring Party: Public Counsel

Case No.: ER-2010-0036

REBUTTAL TESTIMONY

OF

RUSSELL W. TRIPPENSEE

Submitted on Behalf of the Office of the Public Counsel

AMEREN UE ELECTRIC

Case No. ER-2010-0036

February 11, 2010

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.

[illegible]

Russell W. Trippensee
Russell W. Trippensee

A circular notary seal for the State of Missouri. The outer ring contains the text "NOTARY PUBLIC" at the top and "STATE OF MISSOURI" at the bottom, separated by two stars. The center of the seal contains the words "NOTARY" and "SEAL" stacked vertically, with three small dots between them.

Shylah C. Brossier
Shylah C. Brossier
Notary Public

My commission expires June 8, 2013.

REBUTTAL TESTIMONY
OF
RUSSELL W. TRIPPENSEE
AmerenUE
CASE NO. ER-2010-0036

1 **Q. PLEASE STATE YOUR NAME AND ADDRESS.**

2 A. Russell W. Trippensee. I reside at 1020 Satinwood Court, Jefferson City, Missouri 65109, and my
3 business address is P.O. Box 2230, Jefferson City, Missouri 65102.

4 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

5 A. I am the Chief Utility Accountant for the Missouri Office of the Public Counsel (OPC or Public
6 Counsel).

7 **Q. ARE YOU THE SAME RUSSELL W. TRIPPENSEE WHO HAS FILED DIRECT**
8 **TESTIMONY IN THIS CASE?**

9 A. Yes.

10 **Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?**

11 A. To respond to the direct testimony of AmerenUE witnesses Mark C. Birk and Gary S. Weiss who
12 recommend that the Missouri Public Service Commission (MPSC or Commission) authorize an
13 Environmental Cost Recovery Mechanism (ECRM) for AmerenUE. The Commission promulgated
14 and published rules regarding an ECRM in the Missouri Register on July 1, 2009 as a result of
15 Senate Bill 179 (SB179) enacted during the 2005 legislative session.

16 **Q. ARE THE COMMISSION RULES UNDER APPEAL BY ANY PARTIES?**

1 A. Yes. It is my understanding that Public Counsel filed an appeal of the Commission's order of
2 rulemaking that created the ECRM rules. That appeal is pending in the Cole County Circuit Court
3 (Case No. 09AC-CC00336). If that appeal is successful, any ECRM approved under those rules
4 might need to be unwound. Although my main point is that an ECRM is unnecessary for
5 AmerenUE at this time, the fact that the ECRM rules may be overturned is an additional reason not
6 to approve an ECRM in this case.

7 **Q. IS COMMISSION AUTHORIZATION AND IMPLEMENTATION OF AN ECRM FOR**
8 **ELECTRIC UTILITIES MANDATED BY SB179 OR THE COMMISSION RULES?**

9 A. No. SB179 as codified in RSMo 386.266.4 states;

10 The Commission shall have the power to approve, modify, or reject adjustment
11 mechanisms submitted under subsections 1 to 3 of this section only after providing
12 the opportunity for a full hearing in a general rate proceeding, including a general
13 rate proceeding initiated by complaint

14 I have been advised by counsel that this section allows the Commission to authorize an ECRM, but
15 does not mandate it to do so.

16 **Q. DOES PUBLIC COUNSEL RECOMMEND THAT AN ECRM IS APPROPRIATE FOR**
17 **AMERENUE AT THIS TIME AND IN THIS CASE?**

18 A. No. Public Counsel opposes authorization of an ECRM at this time. Public Counsel asserts that an
19 ECRM results in single issue ratemaking and as such should only be used if circumstances are such
20 that rates will remain just and reasonable for ratepayers. Further an ECRM should only be used
21 when environmental costs are continuously and significantly volatile relative to the environmental
22 activities when rates are set, that the environmental costs incurred will not result in additional

1 revenues, that it is not anticipated that other factors will offset the environmental cost volatility and
2 that the timing and amount of environmental expenditures are largely outside the utilities control.

3 **Q. WOULD EXPENDITURES FOR LARGE CAPITAL ADDITIONS NECESSARY TO**
4 **ADDRESS ENVIRONMENTAL ISSUES CREATE THE NEED FOR AN ECRM IN**
5 **YOUR OPINION?**

6 A. If the large capital addition is a single project with a specific in-service date, my response would be
7 that an ECRM is not appropriate for several reasons. The primary reason is that a large single
8 project such as a “scrubber” for a coal fired power plant to reduce SO₂ results in a one-time change
9 in rate base that can be appropriately addressed by existing regulatory mechanisms in a general rate
10 proceeding. A one-time cost change does not represent a volatile cost regardless of size. A second
11 concern regards cash flow. The change in rates under an ECRM is capped at 2.5% per year with
12 the balance of the revenue requirement being deferred and capitalized at the utility’s overall cost of
13 capital (RSMo 386.266.2). While this provides earnings protection for the utility (but does not
14 provide any protection for the ratepayer), capitalization of revenue requirement does not provide
15 cash flows that may be necessary to service the various forms of capital or improve credit metrics.
16 The analysis of these cash flow metrics along with earnings determinations are fundamental
17 components of a general rate proceeding.

18 **Q. WHY IS THE APPROPRIATENESS OF AN ECRM DEPENDENT ON THE**
19 **VOLATILITY OF ENVIRONMENTAL COSTS?**

20 A. This question should be answered on two levels. First, if environmental costs are stable from
21 period to period, those costs can be adequately addressed in the traditional ratemaking process.

1 Only when these costs become volatile should the Commission analyze the financial significance of
2 the volatility to determine if an ECRM should be authorized.

3 The financial significance of the volatility is important because the question the Commission should
4 address is whether the volatility will cause a material change in the return on equity earned by the
5 utility. The Commission rules require the determination of an Environmental Revenue
6 Requirement (ERR). Mr. Weiss proposes such on Schedule GSW-E21 attached to his direct
7 testimony. The ERR like the traditional revenue requirement represents the relationship of all costs
8 incurred to serve a level of customers, be it in total or only for environment costs. The revenue
9 requirement is converted into rates which are used to bill customers. Subsequent to the rate case,
10 the resulting revenues are compared to the costs and investment in rate base. If the return on equity
11 that is calculated from this comparison is reasonable, a rate change is not warranted. In order for an
12 ECRM to be warranted, it should be anticipated that there will be a significant change in the
13 earnings related to the ERR. As mentioned previously, although a single large capital addition for
14 environmental costs can change the ERR significantly, this type of addition can be dealt with
15 through traditional ratemaking processes so as to ensure that ratepayers' total rates are just and
16 reasonable.

17 **Q. DOES MR. WEISS'S CALCULATION OF THE ERR PROVIDE SOME INSIGHT**
18 **INTO WHY A CHANGE IN COSTS MAY NOT RESULT IN A CHANGE IN**
19 **EARNINGS FOR THE ERR?**

20 **A.** Yes. Schedule GSW-E21 clearly sets out the basic components of a revenue requirement. The
21 "return of" investment is found on line 4, Depreciation on Environmental Plant in Service. The
22 "return on" investment is shown on line 5, Return and Income Taxes. The various expenses are set

1 out on lines 6 through 9. I would note that ancillary revenues are included on line 10 as an offset to
2 the ERR. The amount found on each line is subject to change in subsequent years from a rate case.
3 Therefore the only way to determine if the ERR has changed is to look at all of these factors
4 together. This is commonly referred to as the “matching principle”. In his direct testimony, MIEC
5 witness Morris Brubaker used the term “synchronization” to describe this process.

6 A critical point to understand is that while any of these factors can change, one factor is guaranteed
7 to change. The Return and Income Taxes, line 5, will be reduced to reflect the increased
8 Accumulated Depreciation Reserve, line 2, which will increase beginning the first month following
9 the rate case and each month thereafter thus reducing the ERR. Unless other cost components
10 increase to offset the impact of Depreciation and the resulting growth in the Accumulated
11 Depreciation Reserve, the ERR will decline.

12 In Mr. Weiss’s calculation of the ERR, it would take an increase on a annual basis of almost 50% in
13 the listed expenses (lines 6 – 9) to offset the decline in the ERR due to recognition that the
14 ratepayers have provided a “return of” a portion of the Environment Plant in Service (line 1) via the
15 Depreciation found on line 4. This analysis of the ERR should highlight the important principle of
16 matching all relevant factors when setting rates that I previously discussed. While a 50% change in
17 costs would appear to be significant (whether or not it is volatile is another important question to be
18 answered), failure to “match” or “synchronize” all relevant factors of the ERR will result in rates
19 that are not just and reasonable.

20 **Q. WOULD AN ECRM OPERATE SEPARATE AND DISTINCT FROM THE OVERALL**
21 **OPERATIONS OF AN UTILITY WITH REGARD TO FINANCIAL RESULTS?**

1 A. No. It is true that the calculation of rates using an ECRM in conjunction with base rates and
2 possibly a Fuel Adjustment Clause would each be a separate determination; the impact of the
3 revenues generated by each rate will be combined and compared to costs and investment to
4 calculate earnings for use by the investment community and ultimately this Commission's review.

5 **Q. WHAT IS THE SIGNIFICANCE OF THE COMBINATION OF REVENUES FOR**
6 **EARNINGS DETERMINATION IN YOUR PREVIOUS RESPONSE?**

7 A. It highlights the problem that can occur when a regulatory commission sets rates using single issue
8 rate mechanisms such as a Fuel Adjustment Clause or an ECRM in addition to the traditional rate of
9 return process. Single issue rate mechanisms do not use the same test as the rate of return model to
10 ensure that rates are just and reasonable. The test inherent in the rate of return model ensures that
11 the rates approved result in revenues that, when compared to the costs and investment necessary to
12 provide service, provides in a level of earnings that is just and reasonable.

13 **Q. DOES RATE OF RETURN REGULATION ANTICIPATE THAT THE COMPONENTS**
14 **OF THE REVENUE REQUIREMENT WILL CHANGE OVER TIME?**

15 A. Yes. This is especially true if one focuses only on the nominal dollar basis of costs included in the
16 utility revenue requirement. The utility industry is very dynamic and there is no question that costs
17 especially on a nominal basis will vary with the passage of time due to multiple factors. Likewise
18 the revenues a utility earns also vary with time. What is important is the comparison of the actual
19 costs to the actual revenues to determine if the utility was able to achieve an adequate rate of return.
20 Focusing on individual components of the cost structure of a utility is not representative of the
21 overall operations of the utility. Failure to look at all relevant factors (revenues, expenses,

investment, and capital costs) will provide minimal if any insight into the actual earnings of the utility.

Q. CAN YOU PROVIDE SOME EXAMPLES OF CHANGES THAT WOULD IMPACT A UTILITY'S EARNINGS IF YOU LOOKED AT THOSE CHANGES IN ISOLATION?

A. Yes. Increased overtime and cost of living increases would cause payroll expense to increase. Conversely, a voluntary separation plan would decrease the number of employees as compared to the revenue requirement determination. Declining customer levels or usage would have a detrimental impact on earnings to the extent the utility is unable to sell the displaced electricity to other customers or the wholesale market. I could go through each and every line item included in the Staff's Accounting Schedules to provide similar examples.

Suffice it to say, the isolation of any actual expense subsequent to the determination of revenue requirement will undoubtedly have a change in nominal dollars from the expense "built" into the revenue requirement. However, it does not follow however that actual earnings have been affected either positively or negatively. The determination of return on equity is the only financial measure of the relationship between revenues, expenses, investment, and capital costs.

Q. IF YOU ASSUME THAT ACTUAL EXPERIENCE IN THE YEAR SUBSEQUENT TO A GENERAL RATE PROCEEDING DOES IN FACT EXACTLY REFLECT THE REVENUE REQUIREMENT LEVELS OF ALL COSTS AND REVENUES; WILL THE ACTUAL EARNINGS BE THE SAME AS THE RETURN ON EQUITY LEVEL FOUND JUST AND REASONABLE?

1 A. No. The level of actual earnings for the period will be higher than the return on equity level in the
2 general rate proceeding. This occurs because during the period the ratepayer will have paid a
3 “return of” the utility’s investment and this payment is reflected through the recording of
4 depreciation expense which will result in a lower net plant-in-service, thus a lower rate base on
5 which to calculate return on equity. This upwards influence on earnings is always present each and
6 every month the utility operates. This does not mean that earnings will always grow as other
7 revenue requirement components will change. However this should highlight the basis for rate of
8 return regulation requirement to review and determine the relationship between all relevant factors.

9 **Q. SHOULD THE VOLATILITY OF ENVIRONMENTAL COSTS NOT ONLY BE**
10 **SIGNIFICANT ENOUGH TO CHANGE THE ERR AND THUS AN ECRM RATE,**
11 **BUT ALSO BE OF SIGNIFICANT MAGNITUDE TO MATERIALLY EFFECT THE**
12 **OVERALL EARNINGS OF A UTILITY?**

13 A. Yes. The components of the overall cost of service of a utility are all individually and collectively
14 subject to change just as the components of the ERR. When evaluating the need for an ECRM, the
15 Commission must recognize that the components of the ERR are also components of the overall
16 cost of service commonly referred to as the revenue requirement. If a change in the ERR is not
17 anticipated to be of significant magnitude to materially affect the overall earnings of the utility, then
18 there is no need for the ECRM.

19 **Q. HOW WOULD YOU RECOMMEND THAT THE COMMISSION EVALUATE WHETHER**
20 **OR NOT A MATERIAL IMPACT ON THE OVERALL EARNINGS OF A UTILITY**
21 **OCCURS?**

1 A. There is no hard and fast rule on materiality regarding the just and reasonable earnings level of a
2 regulated utility. However past practices by this Commission provide guidance as does a prior
3 agreement with AmerenUE.

4 In evaluating rate of return testimony, this Commission on several occasions has used a “zone of
5 reasonableness” around averages of other commission’s finding regarding the appropriate return on
6 equity. This zone was 100 basis points on each side of the average.

7 In Case No. ER-95-411, AmerenUE (operating as Union Electric at that time) agreed to an
8 Experimental Alternative Regulatory Plan (EARP) that shared excess earnings with customers
9 above a certain level of earnings (12.61%) and did not allow Union Electric to file a rate case unless
10 earnings were below a specified level (10.00%). This created a band of 130 basis points around the
11 midpoint equity return of 11.30%.

12 Each of these examples recognizes that a change from a specific level of earnings does not justify a
13 rate change and provided insight into the level of materiality that has been used by multiple parties
14 including AmerenUE.

15 **Q. WAS THE ORIGINAL EARP RENEWED FOR A SECOND THREE-YEAR PERIOD**
16 **WITH THE AGREEMENT OF AMERENUE?**

17 A. Yes, as part of Case No. EM-96-149, AmerenUE agreed to the same sharing grid described
18 previously.

19 **Q. WHAT IS A BASIS POINT WORTH IN THIS CASE?**

1 A. Each equity basis point is valued at approximately \$465,600 in revenue requirement based on an
2 analysis of the Staff's Accounting Schedules. Therefore the band used in the EARP would equate
3 to \$60,528,000 of revenue requirement.

4 **Q. HAVE YOU REVIEWED THE FORECASTED COMPLIANCE EXPENDITURES**
5 **ATTACHED TO AMERENUE WITNESS BIRK'S DIRECT TESTIMONY?**

6 A. Yes I have.

7 **Q. SPECIFICALLY WHAT BUDGET LEVEL OF ENVIRONMENTAL COSTS DO**
8 **THESE SCHEDULES REFLECT?**

9 A. Schedule MCB-E3 provides both detailed and summary information regarding estimated
10 expenditures for environmental costs over the next twenty years. The schedules break these
11 expenditures down into both capitalized costs and expenses. However the total expenditures in the
12 summary section of each section of Schedule MCB-E3 combine both capitalized costs and
13 expenses. It is critical that readers of this schedule understand that the total cost is not equal to
14 revenue requirement. To obtain the revenue requirement, the revenue requirement impact of the
15 capitalized cost would have to be determined based on the appropriate rate of return, depreciation
16 expense and related reserve, income taxes, and accumulated deferred income taxes.

17 **Q. DOES YOUR REVIEW OF SCHEDULE MCB-E3 LEAD YOU TO BELIEVE THAT**
18 **AN ECRM IS NECESSARY FOR AMERENUE AS A RESULT OF THIS CASE?**

19 A. No it does not. Operation and Maintenance expenses for environmental costs experience
20 fluctuations through 2013 that are not material for a utility the size of AmerenUE. The traditional
21 regulatory process is well suited to address the level of environmental expenses.

1 The capitalized expenditures with exception of the Sioux Scrubbers would fail to generate a
2 revenue requirement impact that exceeds any measure of a “zone of reasonableness” with regard to
3 return on equity I previously discussed.

4 Therefore for purposes of this case, Public Counsel does not recommend authorization of an
5 ECRM.

6 **Q. YOU REFERENCED THE SIOUX SCRUBBERS IN YOUR PREVIOUS ANSWER**
7 **AND INFERRED THAT IT WOULD BE AN EXCEPTION. HOW WOULD PUBLIC**
8 **COUNSEL RECOMMEND THAT THIS MAJOR PLANT ADDITION BE ADDRESSED**
9 **IF AN ECRM IS NOT AUTHORIZED?**

10 A. Public Counsel would agree with Missouri Industrial Energy Consumers witness Maurice
11 Brubaker’s alternative approach found on page 22 of his direct testimony beginning on line 19 and
12 continuing to the next page. Essentially Mr. Brubaker is recommending that the Commission
13 authorize an Accounting Authority Order to allow AmerenUE to capitalize carrying costs and
14 depreciation after the plant addition has gone into service. The carrying costs could be calculated in
15 a manner consistent with the Allowance for Funds Used During Construction (AFUDC) or it could
16 be calculated based on the overall cost of capital found appropriate by the Commission in this case.
17 Use of the AFUDC rate would result in a lower capitalized amount; I recommend using the overall
18 cost of capital rate from this case. I believe that rate is consistent with the earnings impact that
19 would occur under an ECRM. Capitalizing this carrying cost would provide AmerenUE with a
20 “return on” its investment. Inclusion of depreciation expense in the capitalized amount would
21 eliminate the downward pressure on earnings resulting from depreciation expense and ensure that

1 AmerenUE cannot argue that it would not receive a “return of” its investment during the period
2 from the in-service date until a subsequent change in base rates.

3 **Q. ARE THERE OTHER INTANGIBLE BENEFITS TO ADDRESSING LARGE**
4 **CAPITAL ADDITIONS FOR ENVIRONMENTAL COSTS AS YOU AND MR.**
5 **BRUBAKER RECOMMEND?**

6 A. Yes. The primary benefit to the ratepayer is that there would be assurance that the rates they pay
7 are based on a consideration of all relevant factors in determining the revenue requirement. An
8 ECRM requires a revenue requirement determination on a portion of the utility’s operations and
9 investment. It does not provide any assurance that overall rates are just and reasonable and as such
10 should be used only in extreme circumstances.

11 The second benefit is that the AAO process for large capital additions would allow the Staff and
12 other parties adequate time to evaluate the project and determine its in-service status. Consolidation
13 of these efforts into the traditional rate proceeding would be a better use of resources for all parties
14 without any detrimental effect on the utility’s earnings.

15 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

16 A. Yes.