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Revenue Requirements
Witness/Type of Exhibit: Schallenberg/Rebuttal
Sponsoring Party: Public Counsel
Case No.: ER-2019-0335

REBUTTAL TESTIMONY

OF

ROBERT E. SCHALLENBERG

Submitted on Behalf of the Office of the Public Counsel

UNION ELECTRIC COMPANY
D/B/A AMEREN MISSOURI

FILE NO. ER-2019-0335

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that has been Redacted**

January 21, 2020

NON-PROPRIETARY

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UNION ELECTRIC COMPANY d/b/a AMEREN MISSOURI
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1
2 **Q. Please state your name, title and business address.**

3 A. My name is Robert E. Schallenberg. My title is Director of Policy working for the Office
4 of Counsel. My business address is the Governor Office Building, Suite 650, 200 Madison
5 Street, Post Office Box 2230, Jefferson City, Missouri 65102.

6 **Q. Are you the same Robert E. Schallenberg who filed direct testimony in this case?**

7 A. Yes, I am.

8 **Q. What is the purpose of your rebuttal testimony?**

9 A. I will address the direct testimonies and schedules of Ameren Missouri's ("Ameren
10 Missouri" or Union Electric Company (UEC) witnesses, Warren Wood, Laura Moore,
11 Kelly S. Hasenfratz, and John J. Reed.

12 I challenge Ameren Missouri's (Ameren Missouri, UEC, or Company) lack of
13 compliance with the Commission's Affiliate transactions Rules (the rule). 4 CSR
14 4240.20.015 because the amount of affiliate transactions, for which the Company seeks
15 recovery in this case, are not separately identified from normal business transactions.
16 Because of the Company's lack of compliance with the rule, I testify that these affiliate
17 transactions payments should not be have been recorded on Ameren Missouri's books and
18 records. The rule prohibits Ameren Missouri from participating in non-compliant affiliate
19 transactions. If Ameren Missouri wants its electric customers to pay for affiliate
20 transactions costs, the correct approach would have been to make adjustments to its books

1 to reflect these costs and support the costs in its direct testimony with evidence proving
2 the costs justness, reasonableness and prudence.

3 In its Staff Report Cost of Service direct testimony it fails to recognize that Ameren
4 Services Company (AMS') claimed affiliate transactions do not satisfy the rule
5 requirements to prove that the costs are must be either the fully distributed costs (FDC) for
6 UEC to produce the goods or services for itself, or the fair market value (FMV) of the good
7 or service. The Staff also is apparently unaware of the 2013 Supreme Court decision that
8 it may not use a presumption of prudence for affiliate transactions. *Office of the Public*
9 *Counsel v. Missouri Public Service Comm'n and Atmos Energy Corp.*, 409 S.W.3d
10 371(Mo. banc 2013).

11 I also note that, even though Staff has filed a Stipulation and Agreement with AMS
12 recommending the Commission grant AMS a variance from essentially every customer
13 protection in the rule (Case No. EO-2017-0176), that Stipulation has not been presented to
14 the Commission for approval, so it has no effect on this rate case and the requirements in
15 the Commission's current affiliate transactions rule.

16 I will discuss the Company's lack of any evidence to demonstrate that the
17 AMS/UEC affiliate transaction costs do not result in subsidization of AMS has that UEC
18 has always been required by statute to show that its proposed cost changes are just and
19 reasonable.

20 I also explain how auditing affiliate transactions is not feasible without UEC's and
21 AMS' compliance with the rules and especially the recordkeeping requirements of the
22 electric affiliate transactions rule. 4 CSR 4240-20.015 The Company's non-compliance
23 with the rule's requirement for competitive bidding and documentation, especially coupled

1 with AMS's failure to effectively cost and price on a goods-and-services-basis makes
2 determining which of AMS' costs are reasonably and prudently charged to Ameren
3 Missouri's customers difficult. In fact, these deficiencies make the determination of the
4 amount of costs that should be included in rates virtually impossible.

5 A separate, but equally problematic, issue that I discuss is the question of whether
6 the \$200,000,000 of AMS' costs it proposes to charge to its Missouri captive customers
7 have been prudently incurred. In a 2013 Opinion, the Missouri Supreme Court decisively
8 concluded that the Commission may not use its practice of a presumption that costs are
9 prudently incurred for affiliate transactions. *Atmos* 409 S.W.3d 371 at 379.

10 I will address the continuing concern of the AMS' use of Asset Retirement Obligation
11 accounts 374 and 379 regarding its legitimacy and appropriateness in properly assigning
12 UEC construction costs. First, I address the Company's testimony.

14 Warren Wood's Direct Testimony

15 **Q. What are your comments regarding Mr. Wood's direct testimony on page 3, lines 3**
16 **through page 4, line 2?**

17 A. He indicates that rate cases should be filed whenever a rate review indicates an increase or
18 decrease in rates. My view is that the quality of the rate review and each of the factors
19 included in the rate review need to be identified and analyzed before making a proper rate
20 case decision. It is my understanding that Ameren Missouri's update of its initial rate
21 review shows a rate increase is needed instead of the rate decrease in its initial filing.

22 **Q. What is your opinion regarding the nature of this case in light of the Company's**
23 **testimony?**

1 A. Ameren Missouri's current retail rates, both before and after expiration of the Tax Cut and
2 Jobs Act bill credits, are significantly excessive. Ameren Missouri is proposing an
3 extremely insignificant rate decrease. I refer to this case as the three (3) penny rate case as
4 that is the monthly rate reduction planned in the Company's filed case. Their filed case will
5 reduce base retail rates by 32 pennies for a year due to seasonally. Schedule
6 RES-R-1 contains support for my quantification of the impact of the Company's original
7 rate filing.

8 **Q. Did you attempt to verify Mr. Wood's assertion that Ameren Missouri filed this case**
9 **because their rate review showed their rates to be excessive by less than a million**
10 **dollars?**

11 A. Yes. I submitted a Data Request OPC 1000 asking for all documentation used to justify
12 filing this case. I did not expect that the Company would not produce any documentation.
13 Schedule RES-R-2 shows the data requests and Ameren Missouri responses regarding why
14 the Company filed this three (3) penny rate case decrease.

15 **Q. How do you respond to Mr. Wood's testimony about diversity?**

16 A. Mr. Wood testifies that:

17
18 Ameren takes diversity seriously: building a diverse workforce for the future,
19 expanding our expenditures to more diverse suppliers, and serving the diverse
20 needs of our communities are critical to achieving performance leadership in our
21 industry.

22
23 Mr. Wood further discusses the diversity of suppliers on page 7, line 15 through page 8,
24 and line 2 of his direct testimony:

25 These diversity and inclusion efforts extend to our suppliers. As the energy
26 provider for the communities we serve, we believe providing diverse-owned
27 businesses an opportunity to compete in the performance of goods and services
28 for Ameren is a critical component of our company's business strategy. This
29 includes providing equal access and opportunity to all qualified suppliers,

1 including diverse suppliers (e.g. minority-, women-, veteran-, service disabled
2 veteran- and LGBT-owned businesses). This strategy is focused on providing
3 access, development and sustainable opportunities for qualified diverse owned
4 business participation within our organization. In 2018 we exceeded our
5 corporate goal of 19% non-fuel spending with diverse suppliers, finishing with
6 \$624 million in total diverse spending, or 25.2%.

7
8 **Q. What are your comments regarding these statements?**

9
10 A. Ameren Missouri aggressively restricts the market it makes available to other suppliers
11 for opportunities to bid and supply a good or service to the Company. Its diversity and
12 inclusion efforts fail because Ameren Missouri ignores the Commission's affiliate
13 transaction requirements that it must acquire goods and services through a competitive
14 bidding process or demonstrate that competitive bidding is neither necessary nor
15 appropriate. 4 CSR 4240.20.015(3)(A). This rule requirement is designed to prevent AMS
16 from excluding other potential UEC suppliers from the opportunity to do business with
17 UEC. Instead AMS provides a vast majority of goods and services UEC purchases without
18 the benefit of competitive bidding.

19 **Q. What does Mr. Wood say about Missouri's new Plant in Service Accounting (PISA)**
20 **statute?**

21 A. On page 9, line 5 through page 11, page 3. Mr. Wood testifies:

22
23 "When a utility constructs a capital project, it accrues an Allowance for Funds
24 Used During Construction ("AFUDC"), which represents the cost of capital used
25 during construction. Once the project is put into service, the accrual of AFUDC
26 stops and the depreciation of the capital project – including AFUDC – begins. Of
27 course, the utility cannot recover the capital cost of the project or the cost of its
28 depreciation until the next rate case. Depending on the in-service date of the
29 project and the filing of the next rate case, it could be months or even years before
30 the utility can reflect the project costs in its rates.

31
32 **Q. Do you agree with this characterization?**

1 A. No. Mr. Wood omits mentioning how the rate making process, now modified by PISA,
2 addressed the costs of new construction in the rate making process. Prior to PISA,
3 construction costs were offset by the excess recovery of existing plant-in-service costs. The
4 existing plant-in-service costs of interest and profit are never actually incurred in the period
5 new rates are effective. In fact, the day new rates become effective the plant in service costs
6 placed in rates begin declining. This fact is caused by the Company's continuing recovery
7 of depreciation for legacy plant cost over the life of the plant. Another regulatory offset is
8 that future construction causes retirement of existing plant. In such a retirement
9 depreciation expense discontinues but is still included customer rates and being recovered
10 from the utility's ratepayers.

11 Now that new construction costs are being addressed by PISA, the recognition of
12 the declining net-plant balances should be addressed in the rate case to keep the rates just
13 and reasonable. I recommend that 85% of one half of the annual depreciation accrual be
14 use as a rate base offset to provide balances to the modification of prior ratemaking
15 practice. Without the adjustment, Ameren Missouri will overcharge its customers by
16 obtaining PISA benefits, while retaining the benefits of the legacy plant declining.

17 **Q. Do you have anything else to address in Mr. Wood's direct testimony?**

18 A. Mr. Wood testifies that:

19 "We are planning carefully for this future, and planning with our customers in mind.
20 We know we must be innovative and forward-thinking, but we also must be good
21 stewards for our customers. To guide us on this journey, we have established Smart
22 Energy Plan Principles, which you can see in Figure 2 below. At the center of all
23 of our planning is our commitment to deliver value to our customers and our
24 communities."

25
26 But, contrary to that statement the principles shown in "Figure 2" state that the goal is:

27 "Provide Financial Stewardship on Behalf of All Stakeholders," thus, expanding the focus

1 of Ameren’s stewardship beyond customers to “All Stakeholders,” which is much broader
2 focus than just customers and can produce less or no benefit to customers.

3 In this case the Company states its \$1 billion spend on additional plant did not even
4 produce \$1.00 dollar of known and measurable savings. On Staff’s data request 463 **

5
6
7 ** It is my understanding the stewardship should have an accountability aspect
8 related to this function. Schedule RES-R-3 ** **

9 **Ms. Moore’s Direct Testimony**

10 **Q. What are the factors driving this case that are not identified or supported by Ms.**
11 **Moore’s direct testimony and related schedules?**

12 A. Ms. Moore direct testimony does not identify or provide any support for the Ameren
13 Missouri’s affiliate transactions. **
14 ** between Ameren Missouri and Ameren Services
15 Company (AMS) in the test year.

16 **Q. How does this affect the case?**

17 A. Since the Missouri Supreme Court found that Commission’s practice of presumption of
18 prudence cannot be applied to affiliate transactions, the Company must provide some
19 justification for this significant proposed inclusion in rates. There is no evidence that these
20 costs are prudently incurred and are not subsidizing Ameren Missouri affiliates. Ms.
21 Moore direct testimony simply does not address it.

22 **Q. What else in Ms. Moore’s direct testimony do you will address?**

1 A. On the page 6, line 18 through page 7, line 6 of Ms. Moore testifies as to the definition of
2 “revenue requirement”- the annual amount of revenues the Company should be allowed an
3 opportunity to obtain from its customers through its rates. Ms. Moore has provided one
4 of the two definitions used for “revenue requirement.” Her definition has been used by
5 Ameren Missouri for as long as I can recall. However, Staff, and others, also define
6 “revenue requirement” as being the amount current rates need to be increased or decreased.
7 It is important to understand what definition is being used being used by another party to
8 avoid misunderstandings.

9 **Q. What is the next portion of Ms. Moore’s testimony will you be addressing in your**
10 **rebuttal testimony?**

11 A. On page 7, lines 18 through page 8, line 5, Ms. Moore testifies as to Company’s plant
12 accounts being recorded consistent with the Uniform System of Accounts (USOA) as
13 prescribed by the Commission and its Asset Retirement Obligation (ARO) accounts.

14 **Q. Do you have any comments regarding these topics?**

15 A. Yes. Ameren Missouri does not fully comply with the USOA regarding its Asset
16 Retirement Obligations (ARO). Ameren Missouri has no waiver or variance granting it
17 approval for its non-compliance with its USOA requirements.

18 **Q. On page 7, line 18 through page 8, line 5, Ms. Moore’s direct testimony addresses her**
19 **Asset Retirement Obligation (ARO) adjustments. Why did you look into this matter?**

20 A. I discovered the accounting being performed in the ARO accounts was outside the
21 established purposes for these accounts. My attention was first drawn to the accounts when
22 I started to examine the Ameren Missouri annual affiliate transaction report that was
23 submitted to the Commission. I saw a significant charge to Ameren Missouri from AMS,

1 which was being recorded in ARO accounts. My initial inquiries revealed that Ameren
2 Missouri was using these ARO accounts as clearing accounts where costs recorded in the
3 ARO accounts are then charged to Ameren Missouri account 107, Construction Work in
4 Progress (CWIP). These costs would finally be included Plant in Service when the CWIP
5 projects are completed.

6 **Q. What caused you to look into this matter?**

7 A. I first looked into this matter in the Ameren Missouri s Cost Allocation Manual (CAM) in
8 Case No. EO-2017-0176. Schedule RES-R-4 is a copy of Ameren Missouri’s response to one of
9 the data requests in that case. This information shows the amount AMS charged Ameren Missouri
10 and recorded in these accounts for the period 2003 through 2018, the latest information available.
11 This schedule also shows that AMS has increased the amount of indirect overheads to be capitalized
12 dramatically in the test year. The second page of this schedule shows Ameren Missouri current
13 footnote regarding its usage of accounts 374 and 379.

14 **Q. What is the concern with these costs?**

15 A. The costs to be charged to accounts 374 and 379 and ultimately capitalized into Ameren
16 Missouri’s rate base as plant in service are described as indirect overhead capital charges.

17 **Q. What is your concern with AMS charging these costs to accounts 374 and 379 not
18 being indirect overhead capital costs?**

19 A. My concern is that the charges to accounts 374 and 379 are costs that should have been
20 recorded as expenses and are not subject to capitalization. These costs should not be
21 earning a return on and a recovery of these costs, they should have been charged to expense.

22 **Q. What raised your concern?**

23 A. When I looked at a transaction regarding an out-of-town investor meeting costs, I noticed
24 that a portion of these costs were being charged to account 374. I was planning to inquire

1 through a data request about this concern. While trying to find the meeting cost in question,
2 I was searching data regarding the detail of items being charged to account 374. There were
3 a significant number of items that appear to not be eligible to satisfy the FERC criteria to
4 allow capitalization of construction overhead.

5 **Q. What are FERC's USOA criteria, guidelines, direction, or instruction regarding the**
6 **capitalization of construction overheads?**

7 A. The FERC USOA has several sections. These sections are Definitions, General Instructions,
8 Electric Plant Instructions, Operating Expense Instructions, Balance Sheet Chart of Accounts,
9 Balance Sheet Accounts, Electric Plant Chart of Accounts, Income Chart of Accounts,
10 Retained Earnings Accounts, Operating Revenue Chart of Accounts, and Operation and
11 Maintenance Expense Chart of Accounts. The Electric Plant Instructions address the
12 capitalization of construction overheads. The USOA instructions for construction overheads
13 is:

14 *4. Overhead Construction Costs.*

15 A. All overhead construction costs, such as engineering, supervision, general office
16 salaries and expenses, construction engineering and supervision by others than the
17 accounting utility, law expenses, insurance, injuries and damages, relief and pensions,
18 taxes and interest, shall be charged to particular jobs or units on the basis of the
19 amounts of such overheads reasonably applicable thereto, to the end that each job or
20 unit shall bear its equitable proportion of such costs and that the entire cost of the unit,
21 both direct and overhead, shall be deducted from the plant accounts at the time the
22 property is retired.

23 B. As far as practicable, the determination of pay roll charges includible in
24 construction overheads shall be based on time card distributions thereof. Where this
25 procedure is impractical, special studies shall be made periodically of the time of
26 supervisory employees devoted to construction activities to the end that only such
27 overhead costs as have a definite relation to construction shall be capitalized. The
28 addition to direct construction costs of arbitrary percentages or amounts to cover
29 assumed overhead costs is not permitted.

30 C. For Major utilities, the records supporting the entries for overhead construction
31 costs shall be so kept as to show the total amount of each overhead for each year, the
32 nature and amount of each overhead expenditure charged to each construction work
33 order and to each electric plant account, and the bases of distribution of such costs.

1
2 An important take-away from these instructions is that all overheads are not eligible to be
3 capitalized. Overheads must have a definite relation to construction.

4 **Q. What are the items that you viewed that caused your concern that the costs were not**
5 **eligible for capitalization and can only be expensed.**

6 A. I noticed, as described by Ameren Missouri, a United Way lunch, Professional Engineer
7 license, celebration cake, chamber membership, Plattsburg chamber, Lathrop chamber,
8 Clay County EDC, the Leader magazine, Caldwell County News, Holiday Dinner, Boots
9 for Supervisor, Celebrate Ameren, Give away candy for CARES booth @ Celebrate
10 Ameren, IEEE membership renewal, EEI membership, vaccine for Puerto Rico, Potosi
11 Town Hall Meeting, Hoskin Town Hall Meeting, SEMO United Way kickoff, EUEC
12 Registration, CARES, Ellisville, Purchase two monitor stands for Celebrate Ameren, GAB
13 Team, United Way Breakfast, NADUUWG, MEA, Mo. PE License Renewal, Retirement
14 meal, Chicago travel NK battery project, Donation Booster Club Golf Tournament, United
15 Way fundraiser, MMRPC, MEDC conference., Company picnic \$850, YMCA Capital
16 Campaign Meeting, Retirement gift, Lunch Callaway County Commissioner, GOB
17 Retirement Catering-Exec. Dining, Retirement Deposit, Final payment Retirement,
18 Retirement, EEI conference, ALT Forum, Plattsburg Chamber, PE Exam Mileage, Puerto
19 Rico, Puerto Rico, Puerto Rico, Burger March, retirements, retirements, Food for Blues
20 Game in Ameren Box, Food for Cards Game in Ameren Box, Farewell lunch, SEC tickets,
21 retirement cake, retirement, retirement, Professional Society membership, PMP yearly
22 dues, PMP exam fee, P/E Club MEA Conference, Airfare – EPRI Renewable , PMP,
23 \$74.00 Tip from July Cardinal game, EEI conference, Final payment for retirement
24 celebration \$477.85, Executive Dining, Retirement, Take photos of Poles, MEDC

1 Conference, United Way Fundraiser, YMCA Capital Campaign Meeting, Company picnic,
2 and Donation Booster Club.

3 Here, I am not testifying as to whether these items should be recovered in customer
4 rates. But I do dispute whether these costs have a definite relationship to construction and
5 are eligible to be capitalized. I noticed items with project numbers or that are mileage and
6 meals associated work activity. Where the labor was charged the related meals and mileage
7 should also be charged there as well. Costs related to specific projects should be charged
8 to the project and not cleared through account 374.

9 **Q. What is the USOA definition of the costs that should be charged to account 374?**

10 A. The USOA definition for costs to be recorded in account 374 is:

11 **374 Asset retirement costs for distribution plant.**

12 This account shall include asset retirement costs on plant included in the distribution
13 plant function.”

14
15 **Q. What is the significance regarding the circumstances that caused you to discover
16 this issue?**

17 A. It raises a concern regarding effectiveness of Ameren Missouri internal controls. I noticed
18 in the response to Staff Data Request 15 in this case for the Accounting Policies and
19 Procedures, Ameren Missouri did not have any policies. All the policies and procedures
20 appear to be Ameren not Ameren Missouri. This indicates that documentation is needed
21 regarding Ameren Missouri’s requirement to maintain its books and records separate from
22 its affiliates. The showing of compliance with the rule is more difficult based on the fact
23 that AMS, Ameren Missouri’s operator controls the policies and procedures that dictate
24 how Ameren Missouri maintains its book and records separate from its affiliates.

25 **Q. What does Ms. Moore’s Schedule LMM-D17 reflect?**

1 A. Schedule LMM-D17 compares the total electric revenue requirement of \$3,030,811,000
2 with the total electric pro forma operating revenues under the present rates of
3 \$3,031,585,000, including off-system energy sales revenues. It shows that the revenue
4 requirement for the test year is \$774,000 less than the pro forma operating revenues at
5 present rates. The \$3,030,811,000 is the amount of revenues used to set the rates filed in
6 this case and is the level of revenues needed to provide Ameren Missouri an opportunity
7 to collect and recover its cost of service, including an opportunity to recover its cost of
8 capital.

9 **Q. What is your fundamental problem with Ms. Moore's the determinations of any**
10 **amounts in this Schedule?**

11 A. I disagree with an adjustment made in the determination of revenues. The adjustment is
12 referred to on page 18 of her direct testimony where she discusses adjustment number 5.
13 Her testimony states that: "Because new retail rates (resulting from File No. ER-2018-
14 0362) were effective August 1, 2018, Adjustment 5 decreases revenues by \$115,711,000
15 to annualize the effect of those new rates."

16 **Q. Why do you disagree with adjustment 5?**

17 A. An adjustment to annualize the new rates is only appropriate when the item being
18 annualized is expected to continue to occur into the future. Ms. Moore testimony on page
19 7 is correct when she testifies that "it is often necessary to adjust the test year data so that
20 it is more representative of future operating conditions. This requires pro forma
21 adjustments to reflect known and measurable changes."

22 **Q. Why is the adjustment inappropriate?**

1 A. The adjustment is predicated on the basis that the TCJA bill credit will continue into the
2 future. The Commission order approving the Stipulation and Agreement, specifically
3 states, “Upon the conclusion of the next general rate proceeding of Ameren Missouri, the
4 newly introduced credit line item will be removed from the service classification tariffs”.
5 The credit currently reducing customer bills will be removed from tariffs. Thus, the revenue
6 generated by these tariffs will increase as the credit line on those tariffs is removed.

7 **Q. Did Staff also make the same revenue adjustment as the company?**

8 A. Yes.

9 **Q. Do you have the same comments for Staff’s adjustment?**

10 A. Yes.

11 **Kelly Hasenfratz Direct Testimony**

12 **Q. Do you disagree with Ms. Hasenfratz direct testimony?**

13 A. Yes. The cover page for this testimony shows the testimony is to address the issue of
14 “Ameren Services Wages and Benefits.” Since Ameren Missouri and Ameren Services
15 (AMS) are separate entities, it was unclear why AMS wages and benefits would be a topic
16 in an Ameren Missouri cost of service determination. The Commission’s affiliate
17 transaction rules require the Ameren Missouri to competitively bid when the Company
18 purchases information, assets, goods or services from an affiliated entity (i.e. AMS). Or
19 the Company must be able to demonstrate why competitive bids are neither necessary nor
20 appropriate. (20 CSR 4240-20.015 (3) (A). UEC should only use AMS services when
21 AMS’s bid is better than the other competitive non-affiliate bids. The fact that AMS has
22 market based wages and benefits does not indicate that AMS is the best vendor to supply
23 goods and services to Ameren Missouri.

1 **Q. What are your other concerns about Kelly S Hasenfratz's direct testimony?**

2 A. My concern is that this testimony is being offered to support the Company's assertion that
3 the sum of the market price of all inputs of a product would equal the product's fair market
4 price. In other words, the sum of the market price of all inputs to a product equals the
5 market price of the whole product. I disagree that wages or salary with benefits totally
6 represent the costs associated with the labor devoted to any product. My experience is that
7 labor related costs, such as supervisors' salary and benefits, employee credit card expenses,
8 mileage, and office space costs are direct or indirect costs associated with labor devoted to
9 the production of a good or service and must be addressed in pricing the product. The
10 productivity of the cost-to-produce process is as important as the market-price-of-the-
11 product process inputs. For example a seller of product with market based price inputs will
12 not succeed if another seller uses less than market-priced inputs to create the competing
13 price.

14
15 **Mr. Reed's Direct Testimony**

16 **Q. What do you address in Mr. Reed's direct testimony?**

17 A. First he describes his testimony as the "purpose of my direct testimony is to provide my
18 assessment and recommendation pertaining to the reasonableness of Ameren Service
19 Company's ("AMS") services and associated costs billed to Ameren Missouri during the
20 test year." I disagree that Mr. Reed or myself can offer an assessment and recommendation
21 of reasonableness of AMS services unless AMS and Ameren Missouri comply with the
22 Commission affiliate transaction rule.

1 The rule is the standard that defines affiliate subsidization. You compliance with the rule
2 then no affiliate is subsidized by the utility. Non-compliant action is a subsidization of
3 the utilities affiliate. For example, when the utility buys from an affiliate at the price that
4 is greater than it would cost the utility to produce the good or service itself, the utility is
5 subsidizing its affiliate. This is why the rule prohibits Missouri electric utilities from
6 participating in these type of transactions. The process to obtain and maintain a
7 Commission approved CAM is the venue to address differences on how the utility will
8 operate to comply with the rule when the utility cannot show “good cause” or non-
9 compliance is in the best interest of the utility’s customers. The rule already provides a
10 process for non-compliance when the utility can show either “good cause” or non-
11 compliance is in the best interests of the utility’s customers.

12 **Q. On page 3, line 16 through 21, however, Mr. Reed testifies that the Commission**
13 **approved AMS in 1997 saying “[i]n its 1997 order approving the merger of Union**
14 **Electric and CIPS, the Missouri Commission also approved the formation of AMS,**
15 **which is a centralized service company that provides various corporate support**
16 **services to Ameren Corporation (AMC) affiliates at cost.” Is this accurate?**

17 **A.** No. I have found nothing in the Commission’s Order in EM-96- 149 or related
18 Stipulation and Agreement that states the Commission approved the formation of AMS.
19 In fact, the Stipulation and Agreement approved by the Commission’s order has a “No
20 Acquiescence” paragraph 13, that states the none of the signatories shall be deemed to
21 approve or acquiesced to the factors that may underlie the Stipulation and Agreement or
22 for which provision is made in the “Stipulation and Agreement”, Schedule RES-R-5 is a
23 copy of the Commission order in question.

1 **Q. On page 8, line 20 through page 9, line 8 Mr. Reed provides his opinion regarding the**
2 **costs Ameren Missouri would incur if the Company would perform the services on**
3 **their own. Do you agree with him that costs of AMS' services the same as if Ameren**
4 **Missouri were to self-provide the services?**

5 A. No. I cannot agree with Mr. Reed that “the services are, at worst, the same as if Ameren
6 Missouri were to self-provide the services. His opinion is that “it is more likely, however,
7 that due to the economies of scale realized by centralizing the shared services at AMS, the
8 services are provided at a cost lower than if Ameren Missouri were to self-provide the
9 services on a stand-alone basis.” My disagreement is that he does not prove the statement
10 that “is more likely” that “[t]here are inherent efficiencies realized by consolidating
11 common functions at one company, as opposed to requiring each operating company to
12 individually perform each service.

13 However, I am aware of one time AMS did examine this issue with UEC with
14 certain AMS employees were transferred to Ameren Missouri. After this review, no other
15 review has occurred’ RES-R-6 is a copy of the information that supports my testimony.

16 Schedule RES-R-7 is a schedule of AMS FERC Form 60 filing that show AMS’
17 annual billing to Ameren Affiliates. A review of AMS cost performance shows that
18 Ameren Missouri and Ameren Illinois Company are paying the highest percentage
19 (93.27%) of AMS’ total cost. Looking at a period beginning 2005 through 2018, UEC and
20 AIC are paying more to AMS than any previous year. On the other side, AMS costs to
21 operate all non UEC/AIC Ameren entities has near been lower. AMC costs in 2018 are the
22 second lowest the holding company has been charged. The costs of AMS’ operations of

1 non UEC/AIC Ameren entities has shrunk to 6.73% with of AMS total costs. The potential
2 that UEC can do better than AMS is at its highest level but is not being explored.

3 **Q. What else do you challenge in Mr. Reeds direct?**

4 A. Mr. Reed provides his opinion regarding whether affiliate costs charged to Ameren are
5 market based when he testifies on page 9, lines 9 through 14 that:

6 AMS' services are provided at cost, without mark-up or profit, which consist primarily of
7 the wages, salaries, and benefits of AMS employees. The wages, salaries, and benefits
8 AMS pays and provides are market based. Therefore, it is reasonable to conclude that
9 AMS' costs are market based.

10
11 I don't disagree that AMS wages, salaries, and benefits are not market based if not
12 above market. I disagree that AMS costs by themselves establish the Fair Market Price
13 (FMP) for the goods and services charged to Ameren Missouri. The FMP considers more
14 than costs. FMP recognizes the buyer's need and related net benefit to determine whether
15 the seller's price satisfies the buyer's needs.

16 **Q. Do you agree with Mr. Reed's suggestion that it is reasonable to conclude AMS'**
17 **costs are market based?**

18 A. No.

19
20 **Q. Do you agree with Mr. Reed when he testifies surveys are a reasonable substitute for**
21 **determining FMP or FDC?**

22 A. No. On page 9 line 15 through 23 state Mr. Reed states that: "To ensure that the employees
23 are provided a reasonable compensation package, the AMS Human Resources Department
24 routinely benchmarks wages, salaries, and benefits against local, regional, and national
25 companies. Its goal is to provide a total compensation package that is reflective of the
26 market. But this is not the method required by the rule to develop a FMP or a FDC and is
27 contrary to the requirements of the Rule.

1 **Q. Has the Commission accepted benchmarking as an acceptable substitute for rule**
2 **compliance?**

3 A. No. Although Mr. Reed says: “The Company appropriately periodically participates in
4 and reviews the results of benchmarking studies to assess AMS’ costs, as well as Ameren
5 Missouri’s overall operating expenses, AMS has not requested a waiver from the
6 Commission to use “reviews of benchmarking studies” as a substitute for determining FDC
7 or FMP.

8 **Q. Mr. Reed testifies that “Ameren Missouri has formed a CAM team and meets**
9 **extensive reporting and recordkeeping requirements, going well beyond existing**
10 **legislative and regulatory requirements, to continually oversee the dealings between**
11 **AMS and the operating companies. Have you seen any documents to support this**
12 **testimony?**

13 A. No I have not. The results that are being shown on Schedule RES-R-7 show that AMS and
14 Ameren Missouri AMS costs are rising not stabilizing.

15 **Q. Do you agree with Mr. Reed concerning how AMS charges UEC?**

16 A. No. On page 4 line 7, Mr. Reed testifies that; “AMC has no employees and provides no
17 services to Ameren Missouri.” On page 7, line 18 through page 8, line 9, Mr. Reed testifies:

18 AMS direct charges for its services when the service is only to one affiliate?

19 But AMC is the only entity with shareholders and it should be charged for

20 all shareholder services. AMC is UEC’s only shareholder but AMS still

21 incorrectly charges UEC for shareholder services.

1 **Q. When the direct assignment of costs is not possible, are AMS' services provided to**
2 **Ameren Missouri and its other affiliated companies at the fully distributed cost of**
3 **providing those services?**

4 A. Yes, they are (and that is true for directly charged services as well). All costs incurred by
5 AMS are either directly charged (when the cost applies only to one affiliate) or allocated
6 using a service request system. Regardless of whether the services are directly assigned or
7 allocated, the cost of the services is always priced at AMS' fully distributed cost with no
8 mark-up or profit component.

9 **Q. What are your responses to these claim that UEC has any control over service**
10 **requests?**

11 A. The service request system is completely controlled by AMS. UEC does not complete a
12 service request for goods or services, instead AMS provides the good or service and
13 charges it to UEC. Important to the issue of costs AMS assigns to UEC is the fact that the
14 rule judges full distributed cost based on UEC's ability to provide the service for itself
15 rather than AMS' full distributed cost.

16 **Q. Please explain the difference.**

17 A. In his direct testimony in this case Mr. Reed's testifies on page 8 lines 11 through line 17
18 regarding "fully distributed costs;"

19 Section (1)(F) of the Code defines fully distributed cost as "a methodology that
20 examines all costs of an enterprise in relation to all the goods and services that
21 are produced. Fully distributed cost requires recognition of all costs incurred
22 directly or indirectly used to produce a good or service. Costs are assigned either
23 through a direct or allocated approach. Costs that cannot be directly assigned or
24 indirectly allocated (e.g., general and administrative) must be included in the
25 fully distributed cost calculation through a general allocation."
26

1 Mr. Reed neglects to mention the fact that under Section 2 of the rule “Standards”
2 the rule specifies which entity’s fully distributed cost is required to be established:

3 (2) Standards.

4 (A) A regulated electrical corporation shall not provide a financial advantage to
5 an affiliated entity. For the purposes of this rule, a regulated electrical
6 corporation shall be deemed to provide a financial advantage to an affiliated
7 entity if—

8 1. It compensates an affiliated entity for goods or services above the lesser of—

9 A. The fair market price; or

10 B. The fully distributed cost to the regulated electrical corporation to provide
11 the goods or services for itself; or

12 2. It transfers information, assets, goods or services of any kind to an affiliated
13 entity below the greater of—

14 A. The fair market price; or

15 B. The fully distributed cost to the regulated electrical corporation.

16 4 CSR 240-4240.015 (2)(emphasis added)

17 **Q. What opinion does Mr. Reed offer on UEC’s ability to provide the service itself?**

18 A. Mr. Reed on page 8, line 20 through page 9, line 8 provides his opinion regarding the
19 costs Ameren Missouri would incur if the Company would perform the services on their
20 own when he testifies concerning whether the costs of AMS’ services are the same as
21 if Ameren Missouri were to self-provide the services that:

22 The services are, at worst, the same as if Ameren Missouri were to self-provide
23 the services. It is more likely, however, that due to the economies of scale realized
24 by centralizing the shared services at AMS, the services are provided at a cost
25 lower than if Ameren Missouri were to self-provide the services on a stand-alone
26 basis.

27
28 **Q. How do you respond to Mr. Reed’s defense of AMS’ services?**

29 A. There is no documentation or any proof that UEC’s customers have seen lower rates or
30 more efficient provision of service due centralized services. Mere assertion of lower costs
31 absent documentation of an easily measured statistic is of little or no value. Mr. Reed
32 provides his opinion regarding whether affiliate costs charged to Ameren are market based
33 when he testifies on page 9, lines 9 through 14 that:

1 A. Yes. AMS' services are provided at cost, without mark-up or profit, which
2 consist primarily of the wages, salaries, and benefits of AMS employees. The
3 wages, salaries, and benefits AMS pays and provides are market based. Therefore,
4 it is reasonable to conclude that AMS' costs are market based.
5

6 **Q. What does the phrase "it is reasonable to conclude" mean?**

7 A. It means that Mr. Reed is assuming the fact that AMS' costs are market based with no
8 support. He does not provide even basic examples or studies or any other evidence to
9 support his conclusion.

10 **Q. If it were true that the "wages, salaries, and benefits of AMS[s] employees are . . .
11 market based," does that prove the wages, salaries and benefits are precisely the
12 same as UEC's employees would receive for providing the same service?**

13 A. No. The argument that AMS' services are market-based is simply not accurate as I
14 explained in my response to Ms. Kelly Hasenfratz's testimony. There is no documentation
15 that AMS can provide the service at lower cost than UEC could provide the services or
16 incur these labor costs itself.

17 **Q. Mr. Reed testifies that a CAM team has formed and the company meets "extensive
18 reporting and recordkeeping requirements, going well beyond existing legislative and
19 regulatory requirements, to continually oversee the dealings between AMS and the
20 operating companies." This leads him to conclude that Ameren Missouri is "going
21 beyond typical practices in overseeing such dealings, including the use of a dedicated
22 team of employees to oversee CAM compliance, as well as with its reporting activities
23 to monitor and enforce compliance with the requirements set forth in the CAM. How
24 do you respond?**

25 A. What is important is that the Company enforce the requirements of the Commission's
26 Affiliate transactions rules, not its CAM. Ameren Missouri's CAM has never been

1 Commission approved. In my extensive experience at the Commission, UEC has never
2 been in compliance with the rules, so its compliance with the CAM is worthless in
3 determining whether the costs of goods and services UEC receives from AMS involve
4 subsidization or are prudently incurred.

5 **Q. In his testimony Mr. Reed offers his belief that Ameren Missouri would not have been**
6 **able to get goods and services “from an unaffiliated company at lower cost. Do you**
7 **agree?**

8 A. Mere belief without support through studies, detailed documentation and systematic
9 evaluation is worthless. If Mr. Reed were able to testify that AMS had complied fully with
10 the Commission’s affiliate transactions rules and carefully and thoroughly documented its
11 compliance that would be valuable.

12 **Q. On page 10, line 17, Mr. Reed testifies he does not believe that “Ameren Missouri**
13 **would be able to receive the services provided by AMS from an unaffiliated company**
14 **at a lower cost” because AMS follows well-established and well-designed**
15 **procurement policies and procedures that provide for solicitation of competitive bids**
16 **when appropriate so that it is obtaining qualified service providers, and other goods**
17 **it needs to provide its services, at reasonable, market-based prices. How do you**
18 **respond?**

19 A. Mr. Reed does not support his comment that AMS follows procedures that provide “for
20 solicitation of competitive bids when appropriate so that it is obtaining qualified service
21 providers and other goods It needs to provide services at reasonable market based prices”
22 I did not find any documents, workpapers, evidence of benchmarking or other supporting
23 documentation addressing AMS’ regular use of competitive bidding except the very few

1 limited instances mentioned in his testimony at as examples of services outsourced by
2 AMS, on behalf of Ameren Missouri, which include lock box services, printing and
3 distribution of customer bills, certain vegetation management services, and janitorial
4 services.

5 **Staff's Direct Testimony and Report**

6 **Q. What portions of Staff's direct testimony in its Staff Report Cost-of-Service**
7 **(Report) are you addressing in your rebuttal testimony?**

8 A. I am addressing the topics of Ameren Missouri's affiliate transactions and revenue that
9 would be generated from current rates including Lisa Ferguson's direct testimony and the
10 Staff Cost-of-Service Report. The issues raised by the Staff Report are: affiliate
11 transactions (Board of Directors and Lease), corporate allocations, depreciation, and the
12 treatment of the TCJA bill credits. On page 2 of the Staff Report "is an overview of the
13 Staff's revenue requirement determination" where Ms. Ferguson gives her review of all the
14 components that determine Ameren's Missouri revenue requirement Ms. Ferguson does
15 not reference affiliate transactions as one of the primary components.

16 On page 13 Ms. Ferguson identifies issues regarding Corporate Allocations and
17 "Disallowance of all institutional advertising expense, certain dues and donations and
18 miscellaneous expenses and Ameren Corporation board of directors related costs on page
19 14 of the Report. On page 16, neither of these issues, affiliate transactions or corporate
20 allocations is noted as a known and significant issue between Staff and Ameren Missouri.

21 **Q. How do you respond to the Staff's handling of the affiliate transactions and the total**
22 **lack of any mention of affiliate transactions?**

1 A. Staff handled the affiliated transactions in a manner similar with Ameren Missouri in that
2 affiliate transactions are presumed to be prudent until challenged. As stated previously no
3 affiliate transaction is presumed to be prudent and needs an affirmation showing that the
4 affiliate transactions are appropriate and prudent. Both Staff and Ms. Moore made a
5 ratemaking adjustment to remove costs AMS billed Ameren Missouri for AMC expenses.
6 These are expenses incurred by AMS on AMC's behalf that were charged in part to Ameren
7 Missouri and recorded on Ameren Missouri's accounts. Neither Staff nor Ameren Missouri
8 prepared any review to see if there were other inappropriate charges to Ameren Missouri.

9 **Q. What are your concerns with Staff's testimony?**

10 A. This Report lacks the analysis needed to reach a conclusion as to the legitimacy of AMS
11 charges to UEC in the test year. Staff supports the inclusion of over \$200 million in the
12 cost of service study to be used to establish new electric rates in this case. The Report's
13 failed to do any analysis or investigation of the prudence of \$200,000,000 in affiliate
14 transactions costs it proposes to pass to customers. Staff cannot assume that these costs
15 are prudent without verified Company evidence showing the prudence of these
16 transactions.

17 **Q. What is the audit procedure for affiliate transactions?**

18 A. In auditing UEC, Staff may not presume any affiliate transaction to be prudently incurred.
19 In Case No. WA-2019-0299 Staff witness Kim Bolin, and auditor V, testified: "Costs
20 incurred as a result of affiliated transactions between a utility and [its] affiliates are
21 reviewed in detail for prudence during a rate case audit. As part of this review, Staff will
22 request from the Company any bids for services submitted by third parties other than [the

1 utility's] affiliates to determine if the company appropriately explored the option of
2 securing the services at a lower price by using an unaffiliated third party.”

3 **Q. Is UEC's recordkeeping sufficient for Staff to audit affiliate transactions?**

4 A. No. In response to OPC data request 1022, asking “If Ameren Missouri has not used
5 competitive bidding in the acquisition of assets, goods, information and services during the
6 period January 1, 2018 through December 31, 2019, did Ameren Missouri document why
7 the reason competitive bidding was not used? Please provide said documentation,” Mr.
8 Byrne stated “There is no specific documentation . . .” Staff needs such documentation to
9 audit AMS affiliate transactions with UEC for prudence.

10

AFFILIATE TRANSACTIONS

1
2 **Q. In your direct testimony in this case you stated the Company in many ways fails to**
3 **comply with the Commission's affiliate transactions. Here, please discuss the**
4 **problems created when a company does business with its affiliates and does not**
5 **comply with the rules.**

6 A. UEC cannot operate independently.

7 **Q. How do you know?**

8 A. I checked the contract that UEC had with its service company. This contract (GSA) had
9 several elements in its contract inconsistent with the rule's requirement. The Company has
10 never complied with the Commission's requirements to use competitive bidding or be able
11 to demonstrate that competitive bidding is neither necessary nor appropriate. While the
12 Ameren system has purchasing policies and procedures that require competitive bidding or
13 approval not to procure without competitive bidding, these policies and procedures are not
14 applied to the UEC affiliate transactions. The Company has never applied the cost
15 requirements to the goods and services it procures from its affiliates.

16 **Q. Have you worked with the Company to develop a Commission approved Cost**
17 **Allocation Manual (CAM)?**

18 A. Yes. The parties to Case No. EO-2017-0176, UEC, AMS, Commission Staff and the OPC
19 engaged in lengthy discussions about what should be included in a Cost Allocation Manual
20 for submission to the Commission. The resulting Stipulation between the Company and
21 Staff is filed at the Commission but stayed pending the possibility the Commission will
22 change the current affiliate transactions rules. Case No. AW-2018-0394

23 **Q. Is a Commission approved CAM required?**

1 A. Yes. In the Commission affiliate transaction rules evidentiary standards section (3), UEC
2 is required to use a Commission approved CAM in its purchase of affiliate goods and
3 services. The Commission approved CAM sets forth cost allocation, market valuation and
4 internal costs methods. It is these costing standards that allow the Commission to audit
5 and supervise utility companies.

6 **Q. Has the Commission addressed its powers to supervise the activities of monopoly**
7 **utility companies?**

8 A. Yes, in its June 3, 2002 Substitute Brief to the Missouri Supreme Court supporting its
9 affiliate transactions rules the Commission noted that its powers to supervise utility
10 companies is broad: “The Commission has broad power to assure that a utility provides
11 safe and adequate service at just and reasonable rates and no more, and to supervise utilities
12 in the public interest. Section 393.130.1 and Section 393.140(1).” Case No. SC84344
13 Comm’n Br. at p. 36.

14 The Commission further explained that its purpose is to protect ratepayers from
15 the actions of monopoly utilities:

16 In its broadest aspects, the general purpose of such regulatory legislation is
17 to substitute regulated monopoly for destructive competition. But the
18 dominant thought and purpose of the policy is the protection of the public
19 while the protection given the utility is merely incidental.

20 Case No. SC84344 Comm’n Br. at p. 25, *citing De Paul Hosp. Sch. of Nursing*,
21 539 S.W.2d 542, 548 (Mo.App. 1976)(citations omitted).

22
23 The Commission explained the danger inherent in affiliate transactions that
24 captive customers may pay higher than reasonable rates:

25 Affiliate transactions are less than arms-length dealings that may result in
26 consumers paying higher than reasonable rates. The Commission
27 promulgated these Rules because, as a Texas court explained, “affiliate
28 transactions are subject to heightened scrutiny because when a utility and
29 its suppliers are both owned and controlled by the same . . . company, the

1 safeguards provided by arms-length bargaining are absent and ever present
2 is the danger that the utility will be charged exorbitant prices which will, by
3 inclusion in its operating costs, become the predicate for excessive rates.”
4 *Id.* at 32, emphasis added)
5

6 **Q. When had the Commission become aware of the setback on its ability to regulate**
7 **utility companies?**

8 A. It was in a 1975 telephone case involving telephone company rates, the Commission clearly
9 indicated its intention to closely scrutinize utilities operating in Missouri that are part of a
10 holding company structure:

11 The policy which this commission enunciates in this case is that it will not
12 shut its eyes to the facts of such pyramiding and simply look at the legal
13 entity, the Missouri operating company, in determining the level of expense,
14 rate base, revenues, and tax consequences when it is setting the level of rates
15 for the Missouri intrastate operating company.

16
17 This commission recognizes a clear and present danger that affiliated
18 interests can be used to defeat regulation, that to ignore the impact of these
19 affiliated interests is to shirk the commission’s duty and responsibility to
20 examine and consider all facets of a regulated utility’s operations when the
21 commission engages in the ratemaking process. Commission Br. at 39 *citing*
22 *Re United Telephone Co.* Case No. 18,264, 20 Mo.P.S.C. (N.S.) 209, 214
23 (1975)(emphasis added).
24

25 **Q. Which of AMS’ charges to UEC for affiliate transactions practices that are of**
26 **concern?**

27 A. Generally, it is all of AMS’ charges because of discrimination against competitive bidding
28 from third parties to determine the market price for goods and services.

29 **Q. Are any the transactions between AMS and UEC arms-length transactions?**

30 A. They are not. They are affiliate transactions.

31 **Q. Specifically, what are your concerns?**

1 The concern with excessive costs assigned to Missouri ratepayers is broad because of
2 UEC's inability to: 1) to choose which services it receives from AMS contrary to the
3 AMS/UEC contract, 2) determine whether it could provide those services for its customers
4 at a better costs and/or quality rate and 3) to contract with third party vendors to see if it
5 can get the service at a lower price or maybe at a better way. AMS charges all of its costs
6 to its affiliates, but not does provide any documentation showing all the costs AMS charges
7 to UEC should be borne by its Missouri ratepayers as I will discuss below.

8 UEC's failure to comply with the Commission's affiliate transactions rule,
9 including, but not limited to: 1) failure to use FDC as defined by the RULE with its
10 requirement to assign costs to goods and services produced not which affiliate uses the
11 product, 2) FMP consideration to protect against paying more than the good or service is
12 worth to UEC including products not needed by UEC, and 3) protections against being
13 inappropriately charged for the goods or services UEC should be providing for itself or for
14 the goods or services UEC employees perform for AMS.

15 **Q. How is AMS charging UEC for the products it provides?**

16 A. Instead of charging UEC for goods and services provided as required by the Commission's
17 Affiliate Transactions rules, AMS charges are function base and affiliate. If an AMS good
18 or service is only used by one entity, then the costs are supposed to be charged to that
19 entity. If the good or service is needed by more than one Ameren entity then the costs is
20 allocated to these entities on a basis other than how much of the good or service did each
21 entity require. The rule is premised on the supplier affiliate's cost assignment being
22 charged on the portion of the goods and services needed and provided to the entity not

1 based on an allocation of the supplier costs not reflective of the usage of the goods and
2 services in question nor the price benefit of high volume buyer.

3 **Q. What does charging by “function” mean?**

4 A. Function is a category of costs for separate groups of employees. The functions are
5 identified in the Company’s response to OPC data request Schedule RES-R-8.

6 **Q. Why is charging by function not in compliance with the rules?**

7 A. The rule is based on a supplier-buyer basis and cost causer being the cost payer. One of the
8 main concerns with affiliate transaction is the lack of independence and conflict of interest
9 between the utility as a buyer or seller conducting business with an affiliate. For example,
10 the rule prohibits the utility from buying from an affiliate at price that is greater than
11 utility’s costs to provide goods or services for itself. One would not expect a transaction to
12 occur if an independent third party vendor offered the goods and services at a price greater
13 than the utility’s costs to produce the goods and services for itself. Further, one would also
14 not expect a transaction to occur if an independent third party vendor offered the goods and
15 services at a price greater than what the utility could procure the item from an independent
16 third party. On the other hand, affiliate transactions would incentivize the utility to engage
17 in these transactions to increase overall corporate profits at utility customer expense. The
18 rule’s purpose states:

19 “The rule and its effective enforcement will provide the public the assurance that their
20 rates are not adversely impacted by the utilities’ nonregulated activities.”

21 By charging AMS costs to UEC by function based on factors unrelated to UEC’s
22 usage of the function but based on its corporate factors such as capital will result in cost
23 overcharge to UEC.

1 **Q. Why is assigning costs by goods and services rather than by function a superior**
2 **method?**

3 A. This method recognizes the independence that would exist in an arms-length transaction
4 for both UEC, the affiliate buyer and UEC, the affiliate seller. An arms-length transaction
5 is a business deal in which buyers and sellers act independently without one party
6 influencing the other. As an independent buyer would buy or produce the good and service
7 you need at the best price and terms available. An independent buyer would buy a good or
8 service at the best price and terms available. As an independent seller would only sell at
9 the best terms and price they could negotiate. Neither party should have an interest in the
10 consequences of the transaction to the other party.

11 **Q. Does this conclude your testimony?**

12 A. Yes.