

Exhibit No.:
Issues: Alt Reg Plan – Income
Taxes
Witness: Gregory L. Nelson
Sponsoring Party: Union Electric Company
Type of Exhibit: Rebuttal Testimony
Case No.: EC-2002-1
Date Testimony Prepared: May 10, 2002

MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. EC-2002-1

REBUTTAL TESTIMONY

OF

GREGORY L. NELSON

ON

BEHALF OF

**UNION ELECTRIC COMPANY
d/b/a AmerenUE**

Exhibit No. 149
Date 7/10/02 Case No. EC-2002-1
Reporter KRM

**St. Louis, Missouri
May, 2002**

1 **REBUTTAL TESTIMONY**

2 **OF**

3 **GREGORY L. NELSON**

4 **CASE NO. EC-2002-1**

5 **Q. Please state your name and business address.**

6 A. My name is Gregory L. Nelson, and my business address is 1901
7 Chouteau Avenue, St. Louis, Missouri, 63103.

8 **Q. By whom and in what capacity are you employed?**

9 A. I am employed by Ameren Services Company as Vice President & Tax
10 Counsel.

11 **Q. Please describe Ameren Services Company.**

12 A. Ameren Services is a subsidiary of Ameren Corporation that provides
13 various administrative and technical support services for its parent and other subsidiaries,
14 including Union Electric Company doing business as AmerenUE ("UE") and Central
15 Illinois Public Service Company doing business as AmerenCIPS. Ameren Services was
16 formed as a result of the December 1997 merger transaction involving UE and CIPSCO
17 Incorporated,

18 **Q. Please describe your education.**

19 A. I graduated from Vanderbilt University in 1978 with a Bachelor of Arts
20 degree in Business Administration. I also received a Juris Doctor degree from Vanderbilt
21 University in 1981. I received a Master of Laws degree in Taxation from Georgetown
22 University in 1988.

23 **Q. Please describe your qualifications.**

1 A. I have been employed exclusively in the field of taxation since my
2 graduation from law school. My tax experience includes government service (with the
3 Tax Division of the United States Department of Justice in Washington, D.C. from 1984-
4 1988), the private practice of law (with Reid & Priest in Washington, D.C. from 1988-
5 1995) and employment as the head of the UE and Ameren Services Tax Departments
6 (1995-present). Since 1988, my career has been exclusively focused on the taxation of
7 regulated utilities and their associated businesses.

8 I have served as Chair of the Edison Electric Institute's Taxation
9 Committee and presently serve as a Co-chair of that committee's Tax Analysis and
10 Research Subcommittee. I am also the President-elect of the St. Louis Chapter of Tax
11 Executives Institute.

12 I have testified before a subcommittee of the Ways and Means Committee
13 of the United States House of Representatives and various committees of the Missouri
14 Senate and House of Representatives on matters relating to the taxation of regulated
15 utilities. I also have testified before the Illinois Commerce Committee on taxation issues
16 during hearings on the merger transaction involving UE and CIPSCO Incorporated.

17 **Q. Please describe your duties and responsibilities as Vice President &**
18 **Tax Counsel.**

19 A. I am Ameren's chief tax officer, and my department is responsible for all
20 aspects of federal, state and local tax return compliance and planning for the Ameren
21 group of corporations, including UE.

1 **Q. What is the purpose of your testimony?**

2 A. The purpose of my testimony is to explain the income tax calculation
3 employed in UE's proposed new Alternative Regulation Plan ("Alt Reg Plan"). In
4 addition, as part of my testimony, I have prepared an **Executive Summary** attached
5 hereto as Appendix A.

6 **Q. In his Rebuttal Testimony, Mr. Warner Baxter, the Company's Chief**
7 **Financial Officer, has proposed the adoption of the Alt Reg Plan. Are you familiar**
8 **with that proposal ?**

9 A. I am generally familiar with the proposed Alt Reg Plan. More
10 specifically, however, I am familiar with the portions of that plan that concern income
11 taxes.

12 **Q. Before addressing the treatment of income taxes in the Alt Reg Plan,**
13 **please define the term "Schedule M-1" item.**

14 A. On the federal income tax return of UE (or any corporation, for that
15 matter), Schedule M-1 consists of a reconciliation of book income and taxable income.
16 Schedule M-1 items are items of income or expense that are treated differently in
17 computing book income and taxable income.

18 **Q. How are income taxes addressed in the Alt Reg Plan?**

19 A. Income taxes are addressed in the discussion of the determination of the
20 Performance Dividend. The Performance Dividend in each Sharing Period is a function
21 of UE's Missouri electric return on equity ("ROE") in that Sharing Period. In
22 determining the Company's ROE, the Alt Reg Plan lists various specific types of
23 expenses and discusses how they are to be treated. One of these specific expenses is the

1 income tax expense, which is addressed in Section 4. F. iii. (L): "The income tax
2 calculation shall begin with UE's method of computing income tax expense as recorded
3 in UE's books and records" with specified exceptions. Thus, the starting point for the
4 calculation is the income tax expense recorded on UE's financial books and records in
5 accordance with generally accepted accounting principles (UE's "book income tax
6 expense").

7 **Q. Please identify the "exceptions" to the book income tax expense that**
8 **AmerenUE proposes.**

9 A. The exceptions are as follows:

10 (I) The schedule M-1 item for defeasance costs shall be disregarded in
11 computing current and deferred income taxes.

12 (II) For purposes of computing current and deferred income taxes,
13 AFUDC debt shall be treated as provided in the settlement concerning this
14 item for the Sharing Period ending June 30, 1999.

15 (III) The schedule M-1 item for FAS 106 shall be disregarded in
16 computing current and deferred income taxes.

17 (IV) The schedule M-1 item for bad debts shall be disregarded in
18 computing current and deferred income taxes.

19 **Q. What is the reason for these exceptions?**

20 A. These exceptions relate to items that are treated differently for regulatory
21 accounting purposes and for book purposes. In order to construct a regulatory income tax
22 expense calculation, the Schedule M-1 items associated with such items must be
23 disregarded or modified to reflect the regulatory treatment.

1 **Q. Are there any other differences between AmerenUE's book income**
2 **tax expense calculation and the tax expense calculation employed in the proposed**
3 **Alt Reg Plan.**

4 A. Yes, section 4. F. iii. (N) of the proposed Alt Reg Plan provides that the
5 interest deduction for the income tax calculation will be based on the embedded cost of
6 long term debt as applied to the rate base. This is consistent with the standard practice of
7 using interest utilized for ratemaking purposes in place of actual interest for purposes of
8 computing the interest deduction for the regulatory tax expense calculation.

9 **Q. What is the reason for this difference?**

10 A. Interest is treated differently for regulatory accounting purposes than for
11 book purposes. Therefore the interest deduction in the regulatory tax expense calculation
12 must be modified to reflect the interest used for regulatory purposes.

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

14 A. Yes, it does.

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

The Staff of the Missouri Public Service
Commission,)

Complainant,)

vs.)

Case No. EC-2002-1

Union Electric Company, d/b/a)

AmerenUE,)

Respondent.)

AFFIDAVIT OF GREGORY L. NELSON

STATE OF MISSOURI)

) ss

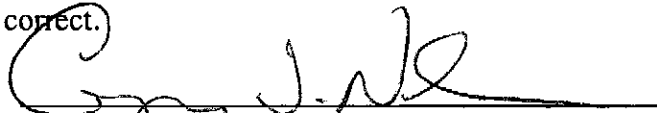
CITY OF ST. LOUIS)

Gregory L. Nelson, being first duly sworn on his oath, states:

1. My name is Gregory L. Nelson. I work in St. Louis, Missouri, and I am employed by Ameren Corporation as Vice President and Tax Counsel.

2. Attached hereto and made a part hereof for all purposes is my Rebuttal Testimony on behalf of Union Electric Company d/b/a AmerenUE consisting of 5 pages and Appendix A which has been prepared in written form for introduction into evidence in the above-referenced docket.

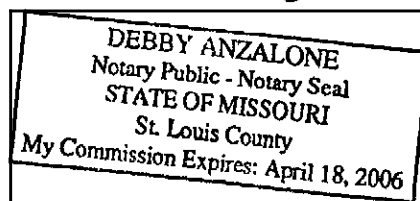
3. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded are true and correct.


Gregory L. Nelson

Subscribed and sworn to before me this 7th day of May, 2002.


Notary Public

My commission expires:



EXECUTIVE SUMMARY

Gregory L. Nelson

Vice President & Tax Counsel of Ameren Services, responsible for all aspects of Ameren's federal and state tax compliance and planning functions

AmerenUE's proposed Alternative Regulation Plan specifically addresses the treatment of income taxes. Under the proposed plan, AmerenUE's income tax expense is taken into account in determining the return on equity, upon which the Performance Dividends are based. For this purpose, income tax expense is the income tax expense as recorded on AmerenUE's books and records, with the following exceptions:

- The Schedule M-1 item (*i.e.*, book/tax difference) for defeasance costs shall be disregarded in computing current and deferred income taxes.
- For purposes of computing current and deferred income taxes, AFUDC debt shall be treated as provided in the settlement concerning this item for the Sharing Period ending June 30, 1999.
- The Schedule M-1 item for FAS 106 shall be disregarded in computing current and deferred income taxes.
- The Schedule M-1 item for bad debts shall be disregarded in computing current and deferred income taxes.

In addition, the interest deduction for the income tax calculation will be based on the embedded cost of long-term debt as applied to the rate base.

These changes to the income tax expense as recorded on AmerenUE's books and records are required to properly reflect items that are treated differently for regulatory purposes and for book purposes. Therefore, the regulatory income tax expense calculation reflects the regulatory treatment of those items.