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Issues: Overview: 4 CSR 240-10.020;
Alternative Regulation Plan
Witness: Robert E. Schallenberg
Sponsoring Party: MoPSC Staff
Type of Exhibit: Surrebuttal Testimony
Case Nos.: EC-2002-1
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MISSOURI PUBLIC SERVICE COMMISSION

UTILITY SERVICES DIVISION

SURREBUTTAL TESTIMONY

OF

ROBERT E. SCHALLENBERG

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

CASE NO. EC-2002-1

Exhibit No. 84
Date 7/10/02 Case No. EC-2002-1
Reporter KRM

*Jefferson City, Missouri
June 2002*

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

The Staff of the Missouri Public Service Commission,)

Complainant,)

vs.)

Union Electric Company, d/b/a AmerenUE,)

Respondent.)

Case No. EC-2002-1

AFFIDAVIT OF ROBERT E. SCHALLENBERG

STATE OF MISSOURI)

COUNTY OF COLE)

ss.

Robert E. Schallenberg, is, of lawful age, and on his oath states: that he has participated in the preparation of the following Surrebuttal Testimony in question and answer form, consisting of 37 pages to be presented in the above case; that the answers in the following Surrebuttal Testimony were given by him; that he has knowledge of the matters set forth in such answers; and that such matters are true and correct to the best of his knowledge and belief.

Robert E. Schallenberg
Robert E. Schallenberg

Subscribed and sworn to before me this 24th day of June, 2002.



Toni M. Charlton
Notary Public

TONI M. CHARLTON
NOTARY PUBLIC STATE OF MISSOURI
COUNTY OF COLE
My Commission Expires December 28, 2004

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1 **SURREBUTTAL TESTIMONY**

2 **OF**

3 **ROBERT E. SCHALLENGER**

4 **UNION ELECTRIC COMPANY**

5 **d/b/a AMERENUE**

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

7 Q. Please state your name and business address.

8 A. Robert E. Schallenberg, 200 Madison Street, Jefferson City, Missouri, 65102.

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

10 A. I am the Director of the Utility Services Division of the Missouri Public
11 Service Commission (MoPSC).

12 Q. Please describe your educational background.

13 A. I am a 1976 graduate of the University of Missouri at Kansas City with a
14 Bachelor of Science degree and major emphasis in Accounting. In November 1976, I
15 successfully completed the Uniform Certified Public Accountant (CPA) examination and
16 subsequently received the CPA certificate. In 1989, I received my CPA license in Missouri.
17 I began my employment with the Missouri Public Service Commission as a Public Utility
18 Accountant in November 1976. I remained on the Staff of the Missouri Public Service
19 Commission until May 1978, when I accepted the position of Senior Regulatory Auditor with
20 the Kansas State Corporation Commission. In October 1978, I returned to the Staff of the
21 Missouri Public Service Commission. Most immediately prior to October 1997, I was an
22 Audit Supervisor/Regulatory Auditor V. In October 1997, I began my current position as
23 Division Director of the Utility Services Division of the MoPSC.

1 Q. Please describe your responsibilities and experience while employed at the
2 MoPSC as Regulatory Auditor V?

3 A. As a Regulatory Auditor V for the MoPSC, I had several areas of
4 responsibility. I was required to have and maintain a high degree of technical and
5 substantive knowledge in utility regulation and regulatory auditing. Among my various
6 responsibilities as a Regulatory Auditor V were:

7 1. To conduct the timely and efficient examination of the accounts,
8 books, records and reports of jurisdictional utilities;

9 2. To aid in the planning of audits and investigations, including staffing
10 decisions, and in the development of Staff positions in cases to which the
11 Accounting Department of the MoPSC was assigned, in cooperation with
12 management and other Staff;

13 3. To serve as lead auditor, as assigned on a case-by-case basis, and to
14 report to the Assistant Manager-Accounting at the conclusion of the case on
15 the performance of less experienced auditors assigned to the case, for use in
16 completion of annual written performance evaluations;

17 4. To assist in the technical training of other auditors in the Accounting
18 Department;

19 5. To prepare and present testimony in proceedings before the MoPSC
20 and the Federal Energy Regulatory Commission (FERC), and aid MoPSC
21 Staff attorneys and the MoPSC's Washington, D.C. counsel in the preparation
22 of pleadings and for hearings and arguments, as requested; and

23 6. To review and aid in the development of audit findings and prepared
24 testimony to be filed by other auditors in the Accounting Department.

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1 The MoPSC relies on the Regulatory Auditor V position to be able to present and
2 defend positions both in filed testimony and orally at hearing. I have had many occasions to
3 present testimony before the MoPSC on issues ranging from the prudence of building power
4 plants to the appropriate method of calculating income taxes for ratemaking purposes. I have
5 worked in the area of telephone, electric and gas utilities. I have taken depositions on behalf
6 of the Missouri Commission. Attached as Schedule 1, is a listing of cases and issues on
7 which I have worked at the MoPSC. My responsibilities were expanded to assist in federal
8 cases as assigned.

9 Q. Have you previously submitted testimony in proceedings before the Federal
10 Regulatory Energy Commission (FERC)?

11 A. Yes. I submitted testimony in Docket Nos. RP94-365, RP95-136, RP96-173,
12 et. al. These are cases involving Williams Natural Gas Company (WNG). WNG provides
13 gas transportation and storage services for local distribution companies serving the western
14 portion of Missouri. WNG provides service to Missouri Gas Energy which serves the
15 Kansas City area. My testimony in Docket No. RP94-365 involved a prudence challenge of
16 the costs that WNG sought to recover in that case. I also filed testimony regarding certain
17 cost of service issues in Docket No. RP95-136, WNG's current rate case before the FERC.
18 These issues included affiliated transactions between WNG and its parent. I filed testimony
19 in Docket No. RP96-173, et. al., on the issue of whether the costs in question met FERC's
20 eligibility criteria for recovery under FERC Order No. 636.

21 I submitted testimony in Docket No. RP96-199. This case is Mississippi River
22 Transmission (MRT) Corporation's current rate case. MRT provides gas transportation and
23 storage services for local distribution companies serving the eastern portion of Missouri.

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1 MRT provides service to Laclede Gas Company which serves the St. Louis area. My
2 testimony in Docket No. RP96-199 involved cost of service issues. These issues included
3 affiliated transactions between MRT and its parent.

4 Q. During your career have you been involved in the negotiation and drafting of
5 agreements between the MoPSC and the utilities under its jurisdiction?

6 A. Yes. I have been involved in negotiations in practically every case in which I
7 have been involved. I have been involved in either the actual drafting of language or the
8 review of language of each stipulation and agreement in these cases related to revenue
9 requirement issues. This experience began with my first rate case involving Kansas City
10 Power & Light Company, in Case No. ER-77-118. In addition, I have been involved in
11 FERC settlement conferences.

12 Q. What is the purpose of your surrebuttal testimony?

13 A. The purpose of this testimony is to respond, in conjunction with other
14 members of the Staff, to certain issues raised by AmerenUE in its rebuttal testimony. My
15 testimony addresses the portions of AmerenUE's rebuttal testimony offered in three areas.
16 The first area is related to general issues raised by the Company in its "overview testimony"
17 and statements made by the Company respecting the Staff's excess earnings/revenues
18 complaint case. The second area is related to the specific issue identified by the Company as
19 "Impact of Rule 4 CSR 240-10.020." The third area is related to issues raised by the
20 Company in its "New Alternative Regulation Plan."

21 **COMPLAINT CASE OVERVIEW**

22 Q. What AmerenUE witnesses will you address in this section of your surrebuttal
23 testimony?

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1 A. I will address the rebuttal testimony of Gary L. Rainwater, Warner L. Baxter,
2 and Craig D. Nelson.

3 Q. What specific issues will you address relating to Mr. Rainwater's rebuttal
4 testimony?

5 A. I will address five issues. First, I will address the dollar amount of Staff's
6 complaint case that Mr. Rainwater discusses on page 2, lines 19 and 20 of his rebuttal
7 testimony. Second, I will address Mr. Rainwater's concepts of "rewarding good
8 performance" and "punishing "good performance" that he discusses on page 3, lines 3
9 through 9 of his rebuttal testimony. Third, I will address Mr. Rainwater's comments on page
10 3, lines 15 through 17 of his rebuttal testimony that the prior four rate reductions are a record
11 of AmerenUE managing costs. Fourth, I will address the methodology that underlies the
12 \$425 million amount that Mr. Rainwater discusses on page 3, line 17 through 19 of his
13 rebuttal testimony as having been provided to customers by AmerenUE since 1995. Finally,
14 I will address Mr. Rainwater's comments regarding the Staff's only motivation in this case
15 and that the "Staff sorely needs senior policy direction and leadership" that appears on page
16 6, lines 3 through 7 of his rebuttal testimony.

17 Q. Mr. Rainwater states on page 2, lines 19 and 20 of his rebuttal testimony that
18 "the Staff would cut AmerenUE's rates by up to \$285 million." Is this statement accurate?

19 A. No. Staff filed its excess earnings/revenues complaint requesting that
20 AmerenUE's rates be reduced up to \$250 million on July 2, 2001. The amount that
21 Mr. Rainwater refers to in his rebuttal testimony is the upper range of the Staff's March 1,
22 2002 cost of service filed in compliance with the Commission's test year order. Staff did not
23 modify its initial complaint request of July 2, 2001 and is not seeking an amount greater than

1 its July 2, 2001 request of up to \$250 million. Regardless, it is important to note that the cost
2 of service study supporting the Staff's complaint will change due to corrections, revisions
3 and modifications made in response to the Company's May 10, 2001 rebuttal testimony.
4 Also, it should be noted that the Office of the Public Counsel (OPC) has proposed additional
5 adjustments that support a greater rate reduction than reflected in Staff's cost of service. It is
6 the Staff's opinion that while the Commission may determine that the ultimate cost of service
7 in this case supports a rate reduction greater than \$250 million, AmerenUE's rates would not
8 be reduced by an amount greater than \$250 million because that is the upper bound of the
9 Staff's complaint filed on July 2, 2001 and no other party has filed a excess
10 earnings/revenues complaint against AmerenUE.

11 Q. Mr. Rainwater discusses on page 3, lines 3 through 9 of his rebuttal testimony
12 his opinion that the Staff is proposing to punish Union Electric for its good performance. Do
13 you agree with Mr. Rainwater's characterization of the Staff's complaint case?

14 A. No. Mr. Rainwater attributes all the excess earnings/revenues in the Staff's
15 case as resulting from management performance especially in the area of managing costs.
16 The Staff's complaint is largely based on reductions in the cost of capital and depreciation
17 rates. Union Electric's cost of capital and depreciation rates were basically established for
18 Union Electric approximately fifteen (15) and twenty (20) years ago, respectively.

19 The Staff's complaint was filed to reduce AmerenUE's current effective rates. These
20 rate levels were actually established during the pre-Callaway and Callaway rate increase
21 cases. Mr. Rainwater attributes the cost of service reductions since 1987 to good
22 management performance. Actually, a significant factor supporting the Staff's complaint case
23 is the fact that Union Electric's load has grown into the capacity that it built in the late

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seventies and mid-eighties. Union Electric consumers experienced significant rate increases due to both the building of this capacity and the rising costs of fuel during that construction period. The following table provides information regarding the rate proceedings that established rates at the level that they are today.

PRE-CALLAWAY

<u>Date Filed</u>	<u>Increase Requested</u>	<u>Increase Granted</u>	<u>Order Date</u>	<u>Case Number</u>
03-04-77	\$ 65,400,000	\$ 30,755,498	01-19-78	ER-77-154
06-06-79	81,600,000	20,473,500 *	04-24-80	ER-80-17
11-26-80	91,000,000	49,975,000 *	07-13-81	ER-81-180
		14,894,493 *	07-31-81	ER-81-180
08-17-81	128,000,000	65,205,000	07-02-81	ER-82-52
12-03-82	122,000,000 ⁽¹⁾	30,500,000	07-06-83	ER-83-163
			03-28-86 ⁽²⁾	

(*) Stipulation and Agreement

(1) Included Callaway II Cancellation Costs

(2) Order On Remand Denying Recovery of Callaway II Cancellation Costs

CALLAWAY

<u>Date Filed</u>	<u>Increase Requested</u>	<u>Increase Granted</u>	<u>Order Date</u>	<u>Case Number</u>
02-15-84	\$ 639,000,000 ⁽¹⁾	\$ 461,065,000 ⁽²⁾	03-29-85	EO-85-17
		652,382,000 ⁽³⁾		ER-85-160

(1) Sixty Five Percent (65%) Increase

(2) One-Time Increase

(3) Increase Over Phase-In Period

During this period, the Commission dealt with the cancellation costs for generating units (e.g., Rush Island Units 3 and 4, Callaway II) that were started but were no longer needed. The rate levels that are at issue in this case were established in the Callaway case wherein AmerenUE sought to place the Callaway nuclear generating station in rate base and start recovering the costs of Callaway in customer's rates essentially. Company witness

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1 Mr. Peter S. Fox-Penner states on page 25, line 10 through 12 of his rebuttal testimony that:
2 "A primary purpose of earnings sharing is to align company and consumer interests and to
3 keep a company's earnings at politically and operationally acceptable levels during the plan's
4 term or commitment period." If "politically and operationally acceptable" had been the
5 criteria for establishing Union Electric's rates during the time period in the above tables, then
6 this excess earnings/revenues complaint case would not be filed because today's rates would
7 not be at their present levels.

8 Staff's complaint case is not punishing the Company for good performance. It is
9 merely providing the consumers some of the benefits that they have paid for over the last
10 fifteen years.

11 In the Callaway rate case shown on the above table, the Commission
12 transitioned/phased in the resulting rate increase over an eight (8) year period. Eight (8)
13 years represented the expected length of time that it would take to remove the excess
14 capacity on the Union Electric system created by the Callaway addition. As the Union
15 Electric load grew and absorbed the excess capacity, the Company's rates would become
16 excessive, as the Company's fixed costs would be spread over a greater number of energy
17 sales. This is a major factor, along with reductions in the cost of capital, that have been
18 contributing to the historical rate reductions for this Company.

19 Q. Has Mr. Rainwater in the past attributed rate reductions to Union Electric's
20 performance when they were the result of other factors?

21 A. Yes. Mr. Rainwater provided direct testimony in Case No. EM-96-149. This
22 case involved the merger between Union Electric and Central Illinois Public Service
23 Company (CIPS). Mr. Rainwater testified that "[a]s 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 occur in 1988, 1989, and 1990." The following table shows the history of the phase-in rates of Callaway:

CALLAWAY PHASE-IN

(In Millions)

<u>Date</u>	<u>Initial Phase-In & Subsequent Rate Changes ⁽¹⁾</u>	<u>Changes for Tax Reform Act of 1986 ⁽²⁾</u>	<u>Complaint Case Rate Changes ⁽³⁾</u>
(Apr 1985)	\$ 138.0	-----	-----
	10.9 ⁽⁴⁾		
(Apr 1986)	112.4	-----	-----
(Apr 1987)	90.1	\$ 57.4	-----
(Dec 1987)	-----	-----	\$ 5.6 ⁽⁵⁾
(Apr 1988)	96.7	60.1	-----
(Apr 1989)	103.7	62.9	-----
(Apr 1990)	111.3	65.8	-----

(1) Per MoPSC Decision (03-29-85) Case Nos. EO-85-19 & ER-85-160

(2) Per UE Motion and Case Nos. AO-87-48, EO-85-17 & ER-85-160

(3) Per MoPSC Decision (12-02-87) Case Nos. EC-87-114 & EC-87-115

(4) Subject to Refund

(5) Effective 12-21-87

The dollar amounts shown in the second column of this table are the result of the initial Callaway decision. The Commission issued a series of orders starting February 11, 1987, respecting Missouri jurisdictional utilities in which individual utilities' rates were reduced or rate increases were reduced as a result of reduced tax liability under the Tax Reform Act of 1986. The reductions resulted from Case No. AO-87-48, which started as a generic proceeding established by the Commission on its own motion to address the Tax Reform Act of 1986. The dollar amounts in the third column reflect the rate increase changes implemented as a result of this docket for Union Electric. The fourth column reflects the changes as a result of the Staff's excess earnings/revenue complaint filing and OPC's

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1 excess earnings/revenues complaint case, Case Nos. EC-87-114 and EC-87-115, against
2 Union Electric. These complaint filings are the cases that Mr. Rainwater discussed in his
3 testimony in Case No. EM-96-149.

4 The Commission noted in its press release following its Report And Order in Case
5 Nos. EC-87-114 and EC-87-115, follows:

6 The Commission's decision is the end result of complaint cases filed
7 by the Public Service Commission Staff and the Office of the Public
8 Counsel against Union Electric. Lower cost of capital (such as lower
9 interest rates), lower fuel process, changes in tax laws (such as the Tax
10 Reform Act of 1986) and increasing demand growth were major
11 factors cited by the PSC in determining the phase-in should end. The
12 Commission's order states, "The evidence shows that the Company's
13 earnings trend is positive. Its revenues are increasing, its fuel costs are
14 decreasing and its rate base is declining. Information reflecting the
15 first six months of 1987 suggests that several categories of expenses
16 are declining and overall it appears that the Company's cost of service
17 is declining." The Commission further noted, "Company's earnings
18 have been shown to be excessive. In this case its current return on
19 equity is being adjusted downward from 15.62 to 12.01 percent." ...

20

21 As a result of federal Tax Reform Act and today's PSC decision, electric rates will
22 have increased by less than half of the amount originally ordered by the Commission in its
23 March 1985 decision to reflect Callaway.

24 Q. Mr. Rainwater states on page 3, line 12 through 22,

25 . . . I believe that our record of cost reduction and service improvement
26 is unmatched in the utility industry and should be commended rather
27 than punished.

28 Consider our record for managing costs. Our Company's last rate
29 increase occurred in 1987, we have made four permanent rate
30 reductions - in 1990, 1993, 1995, and 1998. Since 1995, we have also
31 provided customers more than \$425 million of rate reductions and
32 sharing credits under our alternative rate plans.

33 Are these rate reductions the result of Union Electric managing its cost?
34

A. No, not in entirety. Union Electric did not initiate any of these rate reductions. All of these rate reductions were required because the Commission Staff initiated action that resulted in these rate reductions. Union Electric did not take steps on its own to reduce its rates. The rates in St. Louis and eastern and central Missouri would be higher without the efforts of the Commission Staff along with the help of the parties representing the Company's consumers. The Staff initiated discussions with the Company to determine if a reasonable settlement could be reached and a complaint case avoided in each of these instances. The following table provides more detail regarding these rate reductions.

POST CALLAWAY

<u>Rate Reduction</u>	<u>Date</u>	<u>Case No.</u>	<u>Action That Initiated Rate Reduction</u>
\$ 30,000,000	11-06-90	EM-91-29 EO-87-175	Staff earnings/revenues review as a result of UE purchase of Missouri electric system of Arkansas Power & Light Company. At the same time, there was a Stipulation And Agreement in a UE rate design case that would require a rate reduction on certain customers and an offsetting rate increase on other customers. Stipulation And Agreements in Case No. EM-91-29 and Case No. EO-87-175 permitted a \$30 million rate reduction with no offsetting rate increase.
\$ 40,000,000	01-03-92	ER-93-52	Staff earnings/revenues review to reduce rates for expiration of payments for Callaway Phase-In deferrals.
\$ 30,000,000	07-21-85	ER-95-411	Staff earnings/revenues review. EARP Established in the Stipulation And Agreement.
\$ 16,321,000	02-29-00	ER-96-149	Rate reduction initiated by Staff and OPC as having been negotiated as part of the CIPS merger. Stipulation And Agreement extended the expiration of

the first EARP for three years as a
second EARP to allow retention of
merger savings.

The 1992 rate reduction had nothing to do with Union Electric managing its costs.

This rate reduction was designed to prevent consumers from overpaying for the amortization of the Callaway phase-in deferrals. The Callaway phase-in had two features. First, there was the phase-in of an increase in rates to reach the cost of service determined by the Commission in the Case Nos. ER-85-160 and EO-85-17; the proceedings where Callaway was included in rate base. Second, there was an amortization of the monies that Union Electric did not receive immediately in rates. This amortization was similar to interest on an unpaid balance. Consumers were given in rates the benefit of the reduction in costs after their obligation, the phase-in deferrals, had been satisfied.

There were two significant factors contributing to these rate reductions. First there was the consumer load growth that used the capacity that had been built in the prior years. Second, there was reduction in the cost of capital during this period. Another factor that could contribute to these rate reductions were any merger savings from the merger with CIPS and the purchase of the Missouri electric system of Arkansas Power & Light Company. The status of achieved merger savings is cited by Fitch analysts in their October 2000 "FitchRatings" report on Holding Company-Ameren. The October 2000 "FitchRatings" report provided in response to the Missouri Industrial Energy Consumers Data Request No. 3-6, states that, "Ameren is on target to achieve the announced merger savings of \$759 million (over 10 years), both capital and O & M allocations." These merger savings would apply to the 1998 rate reduction discussed in Mr. Rainwater's testimony. Merger savings is discussed in more detail in Staff witness Mark L. Oligschlaeger's surrebuttal testimony.

1 Q. Is there a problem with Mr. Rainwater's use of the \$425 million amount as it
2 appears in his rebuttal testimony?

3 A. Yes. The \$425 million amount is not comparable to an annual rate deduction
4 amount. There are two types of dollar amounts respecting customer benefits expressed in
5 terms of rate reductions in this case. AmerenUE uses amounts (e.g., \$425 million) that
6 multiplies an annual rate reduction by a number of years and adds the amount of credits
7 applicable to those years. The resulting amount only applies to a specific period of time and
8 will change when a different time period is substituted.

9 The rate reduction amounts used by Staff (e.g., \$ 250 million) are annual amounts
10 that begin the date that they become effective and continue on. For example, a \$250 million
11 permanent rate reduction would exceed AmerenUE's cumulative \$425 amount after two
12 years.

13 Q. Do you have any comments regarding Mr. Rainwater's statements/comments
14 regarding Staff's motivation and the need for senior policy direction and leadership that he
15 discusses on page 6, lines 3 through 7 of his rebuttal testimony?

16 A. Yes. Mr. Rainwater has never spoken or shared his concerns with the Staff
17 before the filing of this testimony on May 10, 2002. The Staff has always tried to make itself
18 available to meet and discuss items of concern with the utilities regulated by the
19 Commission. These meetings have occurred early in the morning and late in the evening to
20 accommodate the needs of the utility representatives. These types of concerns can also be
21 raised directly with the Staff. Such meetings allow the participants the opportunity to engage
22 in serious and open discussions. There are, of course, other forms that a utility may utilize.
23 The only concerns that the Staff has are those respecting *ex parte*.

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1 I can state that this complaint case, as well as all other Staff complaint cases with any
2 utility, have never had a predetermined goal to establish a new record or be as large as it can.
3 For example, the Staff has proposed in this case a forty (40) year amortization of the excess
4 depreciation reserve. A shorter amortization period (e.g., 20 years) would have increased the
5 amount of the Staff's excess earnings/revenues complaint significantly. The Staff did not
6 reflect in its case the \$100 million of value transferred by Union Electric to its nonregulated
7 affiliate, Ameren Generating Company, through the Joint Dispatch Agreement (JDA). The
8 Staff did not raise its complaint above the \$250 million level when its cost of service reached
9 \$286 million in the Staff's March 1, 2001 direct case filing. The Staff's surrebuttal
10 testimony will illustrate other areas (e.g., production plant maintenance) of the Staff's cost of
11 service where the Staff's position could be adjusted to reflect even greater excess
12 earnings/revenues. I acknowledge that the Company and Staff have significant
13 disagreements on a number of issues. However, the Staff has not sought out a disagreement
14 with the Company on any issue because the Staff seeks to "justify the largest rate reduction it
15 can" as Mr. Rainwater suggests.

16 Mr. Rainwater also raises the issue of "Staff sorely needs senior policy direction and
17 leadership." He has not provided any details regarding his concerns. The Staff would have
18 and will meet with him at any time he wishes to discuss this matter or other matters.
19 Mr. Rainwater's concern may be based on areas discussed in the Company's rebuttal
20 testimony. Some of these areas mischaracterize the Staff's position or actions. It is not
21 possible to address Mr. Rainwater's concerns without more specificity.

22 Q. Can you provide an example of Ameren mischaracterizing the actions of the
23 Staff in this case ?

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1 A. Yes. Company witness Mr. Richard A. Voytas discusses on page 44, line 15,
2 through page 45, line 3 of his rebuttal testimony his opinion that Staff, in its dealings with
3 another electric utility, reversed an earlier decision approved by the Commission that
4 highlights the regulatory uncertainty in the state of Missouri that electric utilities must
5 confront. His statements regarding this matter are inaccurate. The Commission's Report And
6 Order in Case No. EM-99-369 involves the matters that Mr. Voytas addresses in his
7 testimony. The Commission placed conditions on its approval in that case. One of the
8 ordered conditions states:

9 This order is in no way binding on the Commission or any party
10 regarding a future rate or earnings complaint case to contest the
11 ratemaking treatment to be afforded the Power Sales Agreement.
12 UtiliCorp United Inc. shall not seek to overturn, reverse, set aside,
13 change or reverse, whether through appeal or the initiation or
14 maintenance of any action in any forum, a decision or order of the
15 Commission which pertains to recovery, disallowance, deferral or
16 ratemaking treatment of any expense, charge, cost or allocation
17 incurred or accrued by MEP Pleasant Hill, L.L.C. or UtiliCorp United
18 Inc. d/b/a Missouri Public Service in or as a result of the Power Sales
19 Agreement on the basis that such expense, charge, cost or allocation
20 has itself been filed with or approved by the Federal Energy
21 Regulatory Commission, or was incurred pursuant to the Power Sales
22 Agreement.

23 This condition shows that the Staff made no commitments regarding the ratemaking
24 treatment that would be afforded this transaction. There was no reversal of an earlier
25 recommendation regarding ratemaking treatment for the unit in question because the
26 recommendation did not address the matter of future ratemaking. The ratemaking issue was
27 deferred to the rate case in which UtiliCorp United Inc. sought recovery of the costs of the
28 Power Sales Agreement.

29 Q. Do you have any comment respecting Mr. Baxter's use of rate comparison
30 studies to show the reasonableness of the Company's rates?

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1 A. Yes. Mr. Baxter discusses this matter on page 20, line 17, through page 25,
2 line 17. To my knowledge, the Commission has not used rate comparison's to determine a
3 level of "just and reasonable" rates in lieu of a cost of service determination.

4 Q. Are rate comparisons a better methodology than cost of service
5 determinations?

6 A. No. There are five reasons that cost of service determinations are superior to
7 rate comparisons. First, there are winners and losers in each rate comparison. Every
8 comparison will have entities that compare favorably (i.e., winners) to other entities
9 (i.e., losers) in the comparison. This is a constant result in any comparison. Comparisons
10 can be of value for informational and monitoring purposes to identify areas that require
11 further study. Most comparisons cannot be determinative because comparisons are made
12 among entities with different particular facts, circumstances and conditions at different points
13 in time.

14 Second, different rate comparisons show different results. Mr. Baxter cites Staff
15 witness Janice Pyatte's Schedule 8 on page 21 of his rebuttal testimony. I asked Anne Ross
16 to file testimony regarding the rate comparison study that she prepares annually based on
17 U.S. Department of Energy-Energy Information Administration information. This rate
18 comparison shows a different result. This rate comparison shows that Union Electric's rates
19 are higher compared to other Missouri investor-owned electric companies.

20 Third, rate comparison losers cite the fundamental problem with rate comparisons
21 whenever the result does not support the position they want. There are always differences
22 among companies used in a rate comparison. Whenever, a utility finds a rate comparison
23 that it doesn't do well in, or doesn't do as well in as it would like, it points to the differences

1 among those compared as an excuse for the unfavorable result. For example, Mr. Baxter
2 notes on page 21 of his rebuttal testimony that Staff witness Janice Pyatte's Schedule 8
3 comparison does not show that Union Electric has the lowest rates in Missouri. He then
4 provides a list of the differences between Union Electric and St. Joseph Light & Power
5 Company (e.g, closer proximity to low-cost coal supplies, lack of sharing credit
6 consideration, difference in service territory, etc.).

7 Fourth, cost of service determinations address the specific differences among utilities
8 by focusing on the specifics of each utility. Cost of service determinations speak to the
9 specific factors influencing the cost to provide service to a particular service territory at a
10 specific point in time.

11 Fifth, cost of service determinations allows high cost companies to stay in business
12 and provide service. Mr. Baxter's Appendix A-10 and AmerenUE witness Dennis L.
13 Weisman's Schedule 2-1 illustrate this point. The retail electric service provider for Los
14 Angeles, San Francisco, or New York could not justify a rate increase based on this schedule.
15 This schedule would appear to indicate that these cities should have their rates reduced to a
16 level comparable to the rates charged in Houston, Texas. There is no consideration in this
17 rate comparison regarding the issue of whether these metropolitan areas can be served at a
18 lower rate or they have unique cost issues that justify these rate differences.

19 Q. What specific issues will you address relating to Mr. Craig Nelson's rebuttal
20 testimony?

21 A. I will address Mr. Nelson's discussion of the Joint Dispatch Agreement (JDA)
22 in his rebuttal testimony from an affiliate abuse perspective and merger detriment basis.
23 AmerenUE transfers its energy at cost to its nonregulated generating affiliate and receives

1 energy from its nonregulated generating affiliate on the same basis. Both entities forego the
2 market value of their energy in this transfer. A nonaffiliated company would only enter into
3 this arrangement if it were to receive similar value compared to its other options.

4 Q. Mr. Nelson discusses on page 16 of his rebuttal testimony that the JDA
5 produces benefits to AmerenUE of around \$3-4 million per year. Doesn't this indicate that
6 the JDA is beneficial to AmerenUE?

7 A. No. AmerenUE is losing approximately \$103 million of the power that it is
8 transferring to its affiliate. This loss is significant in light of the fact that it leads to higher
9 rates in Missouri to support lower rates in other states or higher overall corporate profits.

10 Q. Does AmerenUE recover all of its costs for the energy that it transfers to its
11 affiliate?

12 A. No. AmerenUE does not recover the carrying cost for its coal inventory used
13 to support the energy transfer to its affiliate. This is an issue in this case.

14 Q. Does the nonregulated affiliate transfer capacity to AmerenUE at cost?

15 A. No. When Ameren buys capacity from the nonregulated affiliate its charged a
16 price greater than cost. Staff witness Dr. Michael S. Proctor discusses Staff's concerns with
17 the JDA in his surrebuttal testimony.

18
19 **IMPACT OF RULE 4 CSR 240-10.020**

20 Q. What Ameren UE witnesses will you address in this section of your
21 surrebuttal testimony?

22 A. I will address portions of the rebuttal testimony of Mr. Warner L. Baxter, Ms.
23 Suede Kelly and Mr. Gary S. Weiss. Mr. Baxter discusses this issue beginning on page 60,

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1 line 20, through page 61, line 21 of his rebuttal testimony. This issue is discussed in
2 Ms. Kelly's rebuttal testimony beginning on page 26, line 13, through page 27, line 5.
3 Mr. Gary S. Weiss's rebuttal testimony discusses this issue beginning on page 29, line 8,
4 through page 30, line 17.

5 Q. What is the value of this issue?

6 A. There are three different values that can be assigned to this issue because there
7 are three different interpretations that can be given to the rule. The value of this issue
8 depends on the interpretation of the rule ultimately adopted by the Commission.

9 Q. What are the three different interpretations of the rule and the related value for
10 each interpretation?

11 A. First, AmerenUE interprets the rule to require that income be imputed into
12 Staff's cost of service equivalent to 3% of the depreciation reserve amount and the
13 depreciation reserve is no longer deducted from rate base. Ms. Kelly discusses this
14 interpretation adopted by the Company, on page 26 of her rebuttal testimony. Mr. Baxter
15 refers in his rebuttal testimony to "counsel" providing him advice on this matter and
16 discusses, at page 61 of his rebuttal testimony, the same methodology as Ms. Kelly.
17 Mr. Weiss assigns a value to Ms. Kelly's and Mr. Baxter's interpretation of the rule ranging
18 from \$287 million to \$375.9 million. On page 30, lines 7 through 11 of Mr. Weiss's rebuttal
19 testimony and his Schedule 20, line 22, attached to that testimony. These amounts are
20 reductions to the amounts of excess earnings/revenues identified in the Staff's case. Union
21 Electric interprets that this rule must be applied to it in this manner and in any rate increase
22 proceeding.

1 A second interpretation is that Union Electric has made a showing to the Commission
2 or the Commission has decided on its own "that the rate [of three percent (3%) per annum] is
3 not reasonably and equitably applicable to it [i.e., to Union Electric]" as provided in
4 subsection (4) of the rule. This interpretation would result in no adjustment to the cost of
5 service in this case or in a rate increase case filed by Union Electric.

6 A third interpretation is that the rule requires the Staff in this case or Union Electric in
7 a rate increase case to impute income into its cost of service determination equivalent to 3%
8 of the depreciation reserve amount that meets the qualifications of the rule. I estimate this
9 amount to be \$106,881,350.18. This amount would increase the amount of the excess
10 earnings/revenues contained in the Staff's case and decrease the Union Electric revenue
11 requirement by \$106,881,350.18 in a rate increase case filed by Union Electric.

12 Q. What does this rule state?

13 A. The Commission rules states as follows:

14 4 CSR 240-10.020 Income on Depreciation Fund Investments

15 PURPOSE: This rule prescribes the use of income on investments
16 from depreciation funds and the means for accounting for that income.

17 (1) In the process of determining the reasonableness of rates for
18 service, income shall be determined on the depreciation funds of the
19 gas, electric, water, telegraph, telephone and heating utilities
20 pertaining to their properties used and useful in the public service in
21 Missouri and shall be applied in reduction of the annual charges to
22 operating income of those utilities.

23 (2) The income from the investment of moneys in depreciation
24 funds shall be computed at the rate of three percent (3%) per annum of
25 the principle amount of the depreciation funds.

26 (3) The principle amount of depreciation funds of any such utility,
27 for the purposes of this rule, shall be deemed to be the equivalent to
28 the balance in the depreciation reserve account of any such utility
29 regardless of whether or not any such depreciation reserve account
30 may be represented by a segregated fund ear-marked for that purpose:

1 provided however, that the principal amount of the depreciation funds
2 may be adjusted by the portion(s) of funds which may have been
3 provided under circumstances other than by charges to operating
4 income or otherwise, these adjustments to be subject to the approval of
5 the commission. The terms depreciation funds and depreciation
6 reserve accounts shall be deemed to include the terms retirement funds
7 and retirement reserve accounts.

8 (4) The rate of three percent (3%) per annum referred to in section
9 (3) shall be applied in the case of each gas, electric, water, telegraph,
10 telephone and heating utility of Missouri; provided, however, that
11 modification of the rate may be made upon the commission's own
12 motion or upon proper showing by a utility that the rate is not
13 reasonably and equitably applicable to it.

14 (5) Affected utilities shall prepare and include in their annual
15 reports to the commission commencing with their annual reports for
16 the year 1945, and in such other reports that may be required by the
17 commission from time-to-time, schedules showing for the year or
18 period covered by such reports, the income from the investment of
19 moneys in depreciation funds. The schedules referred to shall be in the
20 form prescribed by this commission and shall include, among other
21 things that may be prescribed: the principle amount of depreciation
22 funds as represented by balances in depreciation reserve accounts; any
23 adjustments of such depreciation funds and accounts with complete
24 details and explanations thereof; and, the amount of the income from
25 the investment of moneys in depreciation funds computed at the rate of
26 three percent (3%) per annum, or such other rate as may be prescribed
27 by order of this commission.

28 (6) The commission shall retain jurisdiction in this matter for the
29 purpose of making any change(s) in the interest rate prescribed in
30 section (2) that may be warranted.

31 AUTHORITY: sections 392.280 and 393.260, RSMo (1986).
32 *Original rule filed Dec. 19, 1975, effective Dec.29, 1975.

33 *Original authority: 392.280 RSMo (1939), amended 1987 and
34 393.260, RSMo (1967).

35 Q. Ms. Kelly, at page 26, line 16, through page 27, line 2 of her rebuttal
36 testimony, and Mr. Baxter, at page 61, lines 1-5 of his rebuttal testimony, both state that the
37 "rule requires the Commission to calculate the return component of a utility's revenue
38 requirement by multiplying the gross rate base (original cost without subtracting accumulated

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1 depreciation) by the authorized rate of return. The revenue requirement must then be
2 reduced to reflect an imputed income of 3% per year on accumulated depreciation." Does
3 the rule contain language that supports this interpretation?

4 A. No. The rule contains no language that requires "the Commission to calculate
5 the return component of a utility's revenue requirement by multiplying the gross rate base
6 (original cost without subtracting accumulated depreciation) by the authorized rate of return."
7 I know from my 25 years at the Commission that this statement is inaccurate. I participated
8 in cases where the Commission has considered fair-value rate base and the corresponding
9 rate of return, and although I generally no longer file testimony in cases, I am made aware of
10 novel positions taken by parties in Staff excess earnings/revenues complaint cases and utility
11 company rate increase cases.

12 The rule does contain language that requires the imputation of income equivalent to
13 3% of the depreciation reserve amount into a case that meets the qualifications of the rule
14 absent a modification of the rate made by the Commission's own motion or upon proper
15 showing by a utility that the rate is not reasonably and equitably applicable to it.

16 Q. Did either of these two witnesses, Ms. Kelly or Mr. Baxter, provide the basis
17 for this interpretation of the rule by Union Electric?

18 A. No. Ms. Kelly had no workpapers, as noted in her response to Staff Data
19 Request No. 4530. Ms. Kelly provided a list of the Commission decisions and the court
20 cases that she reviewed for the purpose of writing her rebuttal testimony in response to Staff
21 Data Request No. 4505. Her response is attached to this testimony as Schedule 2.

22 Mr. Baxter did provide workpapers but they did not contain any material related to
23 this issue.

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1 Q. Did the Staff conduct any research of this rule after it became aware of Union
2 Electric's position in this case?

3 A. Yes.

4 Q. What research did the Staff conduct?

5 A. The Staff conducted research in two areas. First, the Staff researched the
6 development of the rule. Second, the Staff researched the history of the rule related to Union
7 Electric.

8 Q. How was the rule developed?

9 A. The genesis of the rule is the Commission's Report and Order in Case No.
10 10,723, which was effective January 31, 1946. This order cancelled General Order 38-A.
11 The Commission issued an Order on December 19, 1975 directing the Secretary of the
12 Commission "to refile with the Secretary of State of Missouri on or before December 19,
13 1975, a certified copy of all general orders, rules or orders required by Chapter 536, RSMo
14 1969 to be on file therein." On December 19, 1975 the Commission's Secretary filed
15 certified copies of the Commission's rules and regulations with the Secretary of State. This
16 material included the Report and Order in Case No. 10,723. The Report and Order in Case
17 No. 10,723, the Commission's December 19, 1975 order, and the transmittal letter from the
18 Commission Secretary are attached as Schedule 3 to this testimony.

19 Q. What is the history of Union Electric's compliance with this rule?

20 A. Union Electric could not identify any rate case in which it filed using the
21 method contained in 4 CSR 240-10.020 or any annual report filed in compliance with the
22 requirements of this rule. Schedule 4 attached to this testimony is a copy of Staff Data
23 Request No. 179 and Union Electric's response.

1 Staff reviewed the Company's annual reports for the period 1949 through 1958.
2 Union Electric filed a "Special Depreciation Schedule" in its annual reports to the
3 Commission in 1949, 1950, and 1951 but not in the 1952 annual report and thereafter. This
4 "Special Depreciation Schedule" shows an income amount based on a 3% rate as stated in
5 the Commission's Report and Order in Case No. 10,723. In its 1952 annual report, the
6 Company no longer filed this special depreciation schedule but continued to cross out any
7 reference that an asset account (e.g., Utility Plant) balance was less a reserve amount. Union
8 Electric provided its reserves as a footnote to its balance sheet. In its 1958 annual report,
9 Union Electric reported reserves as offsets to plant balances consistent with the process used
10 today. Schedule 5 attached to this testimony is a copy of the Union Electric annual report
11 material that I reviewed.

12 Q. What interpretation of the rule do you believe is appropriate?

13 A. I believe that the Commission has modified the rate for Union Electric
14 through either its own motion or upon proper showing by the Company that the 3% rate is
15 not reasonably and equitably applicable to it in the 1958 or 1959 time period or even
16 sometime thereafter.

17 Q. What is the basis for your opinion?

18 A. I hold this opinion based on two facts. First, Union Electric began reporting
19 the current method (i.e., plant less reserve) in the 1958-1959 time frame. The Commission
20 prescribed the form of its annual report. The Commission, at least implicitly, adopts the form
21 of its annual report. By 1952, the Commission did not require Union Electric Company to
22 report the income associated with the depreciation reserve as specified by the rule. This
23 would be an indication that the Commission made the decision to no longer follow the

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1 process described in the rule. When I joined the Commission Staff in 1976 as an auditor, the
2 Commission had a group of auditors review the annual reports for accuracy and compliance
3 with the Commission rules. I believe that the previously discussed reporting changes in
4 annual reports in the 1952 time frame would have been in response to some action by the
5 Commission.

6 Second, the Commission would have at least implicitly if not explicitly accepted a
7 Union Electric showing "that the rate [i.e., 3%] is not reasonably and equitably applicable to
8 it" when it accepted Union Electric's first rate case using the depreciation reserve as a
9 reduction to rate base. I do not know what case this was, but I believe that it occurred before
10 Union Electric's Case No. ER-77-154. I have attached a copy of the Commission's Report
11 and Order in that case as Schedule 6. This Report and Order shows that the Commission
12 used a net plant or depreciation reserve as an offset to plant balance in both its determination
13 of fair value rate base on page 36 of the Report and Order and original cost rate base on
14 Appendix A, Sheet 2 attached to the Report and Order.

15 Q. If the Commission decides not to adopt this conclusion, then which
16 interpretation of 4 CSR 240-10.020 do you believe is most appropriate?

17 A. The third interpretation that requires the Staff to impute income into its cost of
18 service equivalent to 3% of the depreciation reserve amount that meets the qualifications of
19 the rule, with the depreciation reserve used as a reduction to rate base.

20 Q. Why do you hold that opinion?

21 A. It has been recognized, since at least 1946, that customers are entitled to a
22 reasonable and equitable return for the use of the funds that they provided in the form of
23 depreciation reserves. If the Commission believes that it must impute a 3% income from the

1 depreciation reserve, then the Commission should decide what treatment of the depreciation
2 reserve produces the most reasonable result. The rule does not state that the depreciation
3 reserve cannot be used as a rate base offset as argued by the Company on this issue. The
4 question that must be determined is whether the return that customers receive should be more
5 or less than the Company's return on its investment. I believe it is reasonable to assume that
6 customers should receive a greater return than the Company given their higher borrowing
7 and opportunity costs.

8 Q. Has the Company included any testimony stating that the application of the
9 3% to its depreciation fund with the exclusion of the depreciation reserve as a reduction to
10 rate base produces a reasonable and equitable amount?

11 A. No. The Company witnesses address the issue from the perspective that their
12 treatment of the depreciation reserve is required. They do not state that it produces a just and
13 reasonable result.

14 Q. Did the Commission attempt to rescind this rule?

15 A. Yes. On June 7, 2001 the Commission issued an "Order Finding Necessity For
16 Rulemaking" regarding a proposed rescission of Commission Rule 4 CSR 240-10.20 -
17 Income Depreciation Fund Investments in Case No. AX-2001-634. Laclede Gas Company,
18 Missouri-American Water Company, Missouri Gas Energy, UtiliCorp United, Inc., and
19 Union Electric Company filed comments and requested a hearing on this matter. Most of the
20 comments were against rescission of the rule. Sprint supported the rescission but it was
21 received after the published response time had expired. The Commission withdrew the
22 proposed rescission as a result of the majority of comments.

AMERENUE'S PROPOSED ALTERNATIVE REGULATION PLAN

Q. What portions of the Company's alternative regulation plan proposal will you be addressing?

A. I will be addressing four elements of the Company's proposed "Alternative Regulation Plan" (ARP). First, I will address the overall plan design. Second, I will comment on the basis of the Company's plan for the determination of the proposed "Performance Dividend" (i.e., AmerenUE's books and records). Third, I will address the infrastructure element of the plan. Fourth, I will address the establishment of an economic development fund called by the Company the Ameren Community Development Corporation (ACDC)..

Plan Design

Q. What Ameren UE witness will you address in this section of your surrebuttal testimony regarding the ARP design?

A. I will address portions of the rebuttal testimony of Mr. Warner L. Baxter, specifically Schedule 1 that contains the ARP proposed by AmerenUE.

Q. Are there issues raised in the Company's proposal from the Staff's perspective?

A. Yes. There are five issues that I will address in this section of my testimony. First, the Company has not provided any detail regarding how its present legal arguments regarding the responsibility of the parties and the Commission regarding the two experimental alternative regulation plans (EARPs) are treated in this new proposal. The Staff refers to this issue as the contract issue. It is assumed that the Company's proposal in this proceeding is based on its legal position regarding the two EARPs and, therefore, the

1 Company is requesting, which is now an appeal to the Missouri Western District Court of
2 Appeals, if the Commission approves the Company's ARP proposal.

3 Second, ARP's performance dividend is not an indication or measurement of
4 improved performance on the part of Union Electric. This is the result of two factors. One,
5 ARP is not founded on an established measure(s) that allows the tracking of progress. ARP
6 lacks a starting point to measure the Company's progress. Two, ARP's performance
7 dividend is influenced by weather and external events to the same degree as any
8 improvement in Union Electric's performance. The following table shows the influence of
9 weather on the first EARP's customer credits:

	Year Ending 6/30/96	Year Ending 6/30/96	Year Ending 6/30/96	Three-Year Total	Three-Year Average
Actual Credits	\$ 44 Million	\$ 18 Million	\$ 28 Million	\$ 90 Million	\$ 30 Million
Weather- Normalized Credits	\$12 Million	\$23 Million	\$ 14 million	\$ 49 Million	\$ 16 Million

10
11 The above shows that weather produced about 50% of the credits in the first EARP's three
12 years.

13 Third, ARP does not encourage increasing improvement, if one assumes earnings
14 incentive performance. This is shown by the fact that the higher the earnings, the greater the
15 percentage that the Company must credit to customers. For example, if the Company earns
16 between 12.5% to 15% return on equity, then 50% of these earnings would be credited to
17 consumers. If the Company earns between 15% to 16% return on equity, then 80% of these
18 earnings would be returned to consumers. If one assumes that a sharing of earnings is
19 needed to promote better performance, then this feature of the Company's proposal would
20 result in a disincentive for the Company to improve performance above a certain level. This

1 design is more conducive for promoting an objective of producing greater earnings for lower
2 levels of performance, as measured by return on equity, than promoting the improvement of
3 Company performance.

4 Fourth, the first band of sharing is heavily weighted to the Company's benefit. The
5 first step (i.e., 10.5% to 12.5%) is worth approximately \$79 million. The Company did not
6 provide any forecasts of its expectations regarding its performance under ARP. During
7 EARP, AmerenUE consistently earned above 12.5%. Therefore, ARP is designed for the
8 Company to retain approximately 78% of the earnings in the 10.5% to 12.5% range.

9 Fifth, the initial rate reduction of \$15 million does not bring the Company's rates
10 down to the starting point of the sharing steps. AmerenUE has designed a plan that provides
11 a high probability that it will earn in the second step of its sharing grid, i.e., above 12.5%
12 without any improvement in its performance.

13 **Plan Foundation**

14
15 Q. What Ameren UE witness will you address in this section of your surrebuttal
16 testimony?

17 A. I will address the calculation of the ARP performance dividend as described in
18 Mr. Baxter's Schedule 1 of his rebuttal testimony.

19 Q. Is there a fundamental problem with the Company's proposed calculation of
20 its performance dividend?

21 A. Yes. The Company proposes an inadequate amount of time for the Staff, OPC
22 and any other party to review the Company's performance each year. The calculation of the
23 performance dividend is based on the Company's books and records. ARP is designed based
24 on the Staff (and presumable OPC and any other party) having have no more than 45 days to

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1 review the initial performance dividend calculation and the underlying books and records
2 supporting this calculation. This time period is also in the EARP design and has generally
3 been extended. The 45-day period has been inadequate under EARP. If this feature is
4 enforced with no extensions, then this feature will create a significant incentive for the
5 Company to calculate its performance dividend in the manner that best suits its purposes.
6 This incentive is created by virtue of the fact that detection of questionable items is
7 substantially reduced by the short, inflexible review period available to the Staff (and
8 presumably OPC and any other party).

9 EARP's actual experience provides no assurance that a 45-day review will be
10 adequate. No earnings report was accepted as calculated during EARPs' six years of
11 operation; nor was the Company's initial calculation used in the final determination of the
12 Company's credit liability in any of the five completed years of the two EARPs. The final
13 year of the second EARP is also in dispute. A procedural schedule for the trial of the issues
14 related to the final year of the second EARP was just set on June 20, 2002. The following
15 table shows the magnitude of the differences related to the final year of the second EARP:

Source:	Union Electric's Report	Union Electric's Accrual	Staff Position	OPC Position
Amount	\$ 9 Million	\$ 40 million	\$52 million	\$ 80 million

16
17 The Staff's actual experience with the two EARPs required the Staff to file testimony
18 three out of the last four years, with one case have been taken to hearing. This case is on
19 appeal to the Missouri Western District Court of Appeals.

20 Q. Are there other issues that you have identified with the Company's proposed
21 calculation of its performance dividend?

1 A. Yes. There are three other issues that I would like to address. These issues
2 are ratemaking methodology, affiliate transactions and Company accruals. First, the
3 Company's ARP proposal implicitly requests the Commission to approve the Company's
4 ratemaking decisions without the benefit of the Commission hearing the views of other
5 parties. This can be seen, for example, on Mr. Baxter's Schedule 1-12, subparagraph (E)
6 where the Company's position for the treatment of goodwill advertising is listed. This item
7 would allow AmerenUE to charge all amounts for goodwill advertising in excess of \$1
8 million as an amount to reduce customer credits or the possibility of customers receiving
9 credits.

10 Second, affiliate transactions have a significant impact on the level of earnings
11 recorded on AmerenUE's books. The JDA, interchange sales, and Ameren Services charges
12 entail significant transactions for AmerenUE. For example, the Company is not presently
13 under the Commission's affiliate transaction rules. Ameren Services charged AmerenUE
14 \$161 million in 2001. There is a real need for establishing an affiliate code of conduct and
15 effective safeguards respecting affiliated transactions if the Commission wishes to use an
16 earnings-based alternative regulation plan for AmerenUE.

17 Third, there is the need for additional reporting and understanding regarding
18 significant Company accruals. This case illustrates a significant variance in opinion
19 regarding the accounting for items such as injuries and damages expense, legal expense and
20 environmental expense. There is a definite need for establishing a reporting format for
21 significant Company accruals made during any sharing period to ensure that earnings are
22 properly recorded.

Infrastructure Investment

Q. What Ameren UE witnesses will you address in this section of your surrebuttal testimony?

A. I will address portions of the rebuttal testimony of Mr. Warner L. Baxter. I will specifically address the portion of his rebuttal testimony contained in his Schedule 1-4, line 20 through Schedule 1-5, line 23. The details of the infrastructure commitment is discussed in the testimony of various other AmerenUE rebuttal witnesses.

Q. Is infrastructure investment important to the Staff?

A. Yes. For example, the Staff has included \$225 million for additional capacity for AmerenUE in its case. The Staff has built into its case an 18% capacity reserve margin.

Q. What is the infrastructure investment component of the Company's ARP.

A. If the Commission accepts the Company's ARP proposal, Mr. Baxter's Schedule 1 states, "UE commits to undertake commercially reasonable efforts to make a minimum of \$1.5 billion to \$1.75 billion of infrastructure investments from January 1, 2002 through June 30, 2005." (Mr. Baxter's rebuttal testimony, Schedules 1-4 and 1-5). This commitment includes investments such as:

- 700 MW of new regulated generation capacity
- Generation plant upgrades that will ultimately result in 270 MW of additional generating capacity
- Replacement of Callaway's steam generators
- Replacement of Venice power plant capacity
- Sioux power plant environmental pollutants controls
- New transmission lines or upgrades that will increase import capability by 1,300 MW
- Various transmission and distribution upgrades

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1 Q. Has the Commission had prior experience with investment commitments in
2 other alternative regulation plans?

3 A. Yes. The Commission had investment commitments related to the
4 Southwestern Bell Incentive Regulatory Experiment (SBIRE) and the Commission's
5 settlement of Case No. TC-93-224, which was the Staff's second excess earnings/revenues
6 complaint case against Southwestern Bell.

7 Q. What knowledge was gained by this experience?

8 A. It is preferable to specify projects not dollars. Dollar commitments promote
9 overspending. Dollar commitments do not promote the efficient expenditure of capital
10 because the approach becomes that since there is money available, it must be spent. Dollar
11 commitments create an inefficient procedure whereby the company must seek a waiver not to
12 spend money, if it finds that necessary projects can be funded more efficiently than had been
13 earlier anticipated.

14 Q. Can you provide options related to AmerenUE that illustrate this point?

15 A. Yes. The AmerenUE Illinois load can be transferred to CIPS, thus dedicating
16 more of the AmerenUE units to Missouri. This option would significantly reduce the amount
17 of capital expenditures needed by AmerenUE. Another option would be to consider the
18 transfer of excess generation from Ameren Energy Generating Company to AmerenUE to
19 allow Ameren to avoid unnecessary expenditures.

20 Q. How does the Company's infrastructure commitment compare to the expected
21 level of construction expenditures?

22 A. Union Electric makes quarterly filings with the U.S. Securities and Exchange
23 Commission (SEC). These reports are referred to as "10-Q" filings. The first quarter for the

1 year 2002 ends on March 31, 2002 and UE's first quarter 20002 10-Q was filed on May 28,
2 2002. In this filing the Company provides its expectation for construction expenditures for
3 the year 2002. Union Electric states on page 15 and 16 of its 10-Q report that its "capital
4 expenditures are expected to approximate \$500 million in 2002." This level of construction
5 will fulfill one-third or 33% of the Company's infrastructure commitment in its rebuttal
6 testimony. Actually, Union Electric is committing to spend \$1 billion for construction in the
7 January 1, 2003 through June 30, 2005 time frame. This would require Union Electric to
8 spend an average of \$400 million annually during this time frame. This amount of
9 construction is consistent with the amount cited by Fitch analysts in the March 13, 2002
10 "FitchRatings" report concerning AmerenUE. This report was provided in response to the
11 Missouri Industrial Energy Consumers Data Request No. 3-6. This report states that:

12 Capital expenditures are forecasted at about \$400 million annually
13 over the next four years. Environmental expenditures account for
14 about \$40 million annually. The level of internal cash generation will
15 be affected by the outcome of the pending rate case; however, the
16 strong capital structure provides significant financial flexibility.

17 AmerenUE's commitment is comparable to its current anticipated level of
18 construction expenditures.

19 Q. How does this commitment compare with Union Electric's historical level of
20 construction expenditures?

21 A. The new commitment would be less than the amount of construction
22 expenditures made in 2001 or expected for 2002. The new commitment would be more than
23 the level of construction before 2001. For the period 1991 through 1995, Union Electric
24 spent on average approximately \$278 million for construction each year. For the period 1996
25 through 2000, Union Electric spent on average approximately \$274 million for construction

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1 annually. In the year 2001, Union Electric spent \$586 million on construction. Union
2 Electric will need to make construction expenditures independent of an ARP.

3 **Economic Development Fund**
4

5 Q. What AmerenUE witnesses will you address in this section of your surrebuttal
6 testimony?

7 A. I will address portions of the rebuttal testimony of Mr. Richard J. Mark that
8 discuss the Economic Development Program proposed by AmerenUE. Mr. Mark discusses
9 the program beginning on page 6, line 5, through page 7, line 16. Mr. Mark also provides
10 information in his Schedule 2, regarding the Ameren Community Development Corporation
11 (ACDC) that would administer the program.

12 Q. What is the Staff's understanding of this program?

13 A. Ameren Community Development Corporation would be controlled by at
14 least six directors with one director being a Ameren employee. The Ameren employee
15 would be an employee of Union Electric or one of its affiliates. The Board of Directors
16 would elect three officers. These positions would be President, Secretary, and Treasurer. A
17 Vice President position is listed in section C of Article VI shown on Schedule 2 to Mr.
18 Mark's rebuttal testimony. The directors and officers would receive reasonable
19 compensation for services rendered.

20 Q. What is Staff's position regarding the establishment of the proposed Ameren
21 Community Development Corporation?

22 A. The Staff recommends that this program not be approved until enough
23 information is available to determine whether proper controls are in place to ensure that no
24 inappropriate expenditures are made by ACDC. This program would be supported by

1 ratepayer funds. It is important to have adequate assurances that the funding of the program
2 is justified by the expected benefits and operation of the proposed entity.

3 Q. What are Staff's concerns regarding this proposed program?

4 A. There are not enough details provided by AmerenUE to determine that the
5 program will produce benefits commensurate with its expenditures. There is no indication
6 that there would be controls in place to ensure that inappropriate or unproductive
7 expenditures would not be made. Presumably, the Commissioners would be interested in
8 knowing what liability, if any, they might have since they would approve the funding of this
9 program. This Staff evaluation is limited because the details of what might constitute
10 acceptable grants have not been provided. Further, there is no information regarding controls
11 on the expenditures after the grants are awarded. The initial success of this program would
12 require a significant time commitment from the directors and officers to ensure the efficient
13 operation of this entity.

14 Q. What additional information would be helpful?

15 A. It would be helpful to discuss the objectives of this program with the
16 individuals that are advocating the establishment of the Ameren Community Development
17 Corporation. I have participated in discussions with Ameren representatives regarding the
18 issue of effective controls and support for this program. I believe that these meetings are an
19 acknowledgement of the need for controls. Specific controls cannot be developed until a
20 greater understanding is developed regarding the type of grants that are intended to be
21 accepted for funding by this entity.

22 The individuals that are likely to be chosen to be directors would be a good source of
23 information, in the event that the details regarding acceptable grants is not known at this

Surrebuttal Testimony of
Robert E. Schallenberg

1 time. These individuals could be interviewed to get their thoughts regarding this question.
2 Appropriate controls can then be designed to provide reasonable assurance that the program
3 will support appropriate, effective and efficient activities.

4 Q. Does this conclude your surrebuttal testimony?

5 A. Yes.

RATE CASE PROCEEDING PARTICIPATION

ROBERT E. SCHALLENGER

<u>COMPANY</u>	<u>CASE NO.</u>
Southwestern Bell Telephone	TR-79-213
Southwestern Bell Telephone	TR-80-256
Southwestern Bell Telephone	TR-81-208
Southwestern Bell Telephone	TR-82-199
Southwestern Bell Telephone	TR-83-253
Southwestern Bell Telephone	TR-86-84
Southwestern Bell Telephone	TC-89-14
Southwestern Bell Telephone	TO-89-56
Southwestern Bell Telephone	TR-90-98
Southwestern Bell Telephone	TC-93-224
Southwestern Bell Telephone	TO-82-3
Kansas City Power & Light Company	ER-77-118
Kansas City Power & Light Company	ER-78-252
Kansas City Power & Light Company	ER-80-48
Kansas City Power & Light Company	ER-81-42
Kansas City Power & Light Company	ER-82-66
Kansas City Power & Light Company	HR-82-67
Kansas City Power & Light Company	ER-83-49
Kansas City Power & Light Company	EO-85-185
Kansas City Power & Light Company	ER-85-128
Missouri Public Service	ER-78-29
Missouri Public Service	GR-78-30
Missouri Public Service	ER-90-101
General Telephone	TM-87-19
General Telephone	TR-86-148
General Telephone	TC-87-57
General Telephone	TR-89-182
Gas Service Company	GR-78-70

Gas Service Company	GR-79-114
Union Electric	EC-87-114
Kansas Power & Light Company	GR-91-291
Kansas Power & Light Company	EC-91-213
Western Resources	GR-93-240
Western Resources	GM-94-40
United Telephone Company of Missouri	TR-80-235
St. Joseph Light and Power Company	EC-92-214
St. Joseph Light and Power Company	ER-93-41
Kansas Power and Light Company	EM-91-213
Laclede Gas Company	GR-94-220
Williams Natural Gas Company	RP94-365-000
Williams Natural Gas Company	RP95-136-000
Mississippi River Transmission	RP96-199-000
Union Electric	EO-96-14
Laclede Gas Company	GT-2001-329

**CASE SUMMARY OF INVOLVEMENT
OF
ROBERT E. SCHALLENGER**

Gas Service Company

Case No. GR-79-114

Date: June 15, 1979

Areas: Deferred Taxes as an Offset to Rate Base

Missouri Public Service Company

Case Nos. ER-78-29 and ER-78-30

Date: August 10, 1978

Areas: Fuel Expense, Electric Materials and Supplies, Electric and Gas Prepayments,
Electric and Gas Cash Working Capital, Electric Revenues

Missouri Public Service Company

Case Nos. ER-79-60 and GR-79-61

Date: April 9, 1979

Areas: Depreciation Reserve, Cash Working Capital

Southwestern Bell Telephone Company

Case No. TR-79-213

Date: October 19, 1979

Areas: Income Taxes, Deferred Taxes

Kansas City Power & Light Company

Case Nos. ER-80-48 and ER-80-204

Date: March 11, 1980

Areas: Iatan, Interest Synchronization, Allocations

Kansas City Power & Light Company

Case No. ER-81-42

Date: March 13, 1981

Areas: Iatan (AEC Sale), Normalization vs. Flow-Through, Allocations, Allowance for
Known and Measurable Changes

Southwestern Bell Telephone Company

Case No. TR-80-256

Date: October 23, 1980

Areas: Flow-Through vs. Normalization

United Telephone Company of Missouri

Case No. TR-80-235

Date: December 1980

Areas: Rate of Return

Southwestern Bell Telephone Company

Case No. TR-81-08

Date: August 6, 1981

Areas: License Contract, Flow-Through vs. Normalization

Kansas City Power & Light Company

Case Nos. ER-82-66 and HR-82-67

Date: March 26, 1982

Areas: Indexing/Attrition, Normalization vs. Flow-Through, Deferred Taxes as an Offset to Rate Base, Annualization of Amortization of Deferred Income Taxes, Cost of Money/Rate of Return, Allocations, Fuel Inventories, Iatan AFDC Associated with AEC Sale, Forecasted Coal and Natural Gas Prices, Allowance for Known and Measurable Changes

Southwestern Bell Telephone Company

Case No. TR-82-199

Date: August 27, 1982

Areas: License Contract, Capitalized Property Taxes, Normalization vs. Flow-Through, Interest Expense, Separations, Consent Decree, Capital Structure Relationship

Kansas City Power & Light Company

Case No. ER-83-49

Date: February 11, 1983

Areas: Test Year, Fuel Inventories, Other O&M Expense Adjustment, Attrition Adjustment, Fuel Expense-Forecasted Fuel Prices, Deferred Taxes Offset to Rate Base

Kansas City Power & Light Company

Case Nos. EO-85-185 and ER-85-28

Date: April 11, 1985

Areas: Phase I - Electric Jurisdictional Allocations

Date: June 21, 1985

Areas: Phase III - Deferred Taxes Offset to Rate Base

Date: July 3, 1985
Areas: Phase IV - 47% vs. 41.5% Ownership, Phase-In, Test Year/True-Up, Decision to Build Wolf Creek, Non-Wolf Creek Depreciation Rates, Depreciation Reserve, Jurisdictional Steam Allocation/Grand Avenue Station

Southwestern Bell Telephone Company

Case No. TR-83-253

Date: September 23, 1983

Areas: Cost of Divestiture Relating to AT&T Communications, Test Year, True-Up, Management Efficiency and Economy

Generic - Straight Line Equal Life Group and Remaining Life Depreciation Methods

Case No. TO-82-3

Date: December 23, 1981

Areas: Depreciation

General Telephone Company of the Midwest

Case No. TM-87-19

Date: December 17, 1986

Areas: Merger

General Telephone Company of the Midwest

Case No. TC-87-57 (TR-86-48)

Date: December 1986

Areas: Background and Overview, GTE Service Corporation, Merger Adjustment, Adjustments to Income Statement

Southwestern Bell Telephone Company

Case No. TR-86-4

Date: None

No prefiled direct testimony

Union Electric Company

Case No. EC-87-114

Date: April 27, 1987

Areas: Elimination of Further Company Phase-In Increases, Write-Off of Callaway I to Company's Capital Structure.

Western Resources

Case No. GM-94-40

Date: November 1993

Areas: Jurisdictional Consequences of the Sale of Missouri Gas Properties

Kansas Power & Light Company

Case No. EM-91-213
Date: April 1991
Areas: Purchase of Kansas Gas & Electric Company

Laclede Gas Company
Case No. GR-94-220
Date: July 1994
Areas: Property Taxes, Manufactured Gas Accruals, Deregulated Cost Assignments

Williams Natural Gas
Docket No.: RP94-365
Date: November 9, 1995
Areas: Imprudence of pipeline decisions that led to the incurrence of gas supply realignment costs.

Williams Natural Gas
Docket No.: RP-95-136
Date: November 30, 1995 and June 14, 1996
Areas: Depreciation and amortization expenses and the Administrative & General (A&G) expenses, including expenses relating to affiliate transactions.

Mississippi River Terminal Corporation
Docket No.: RP96-199
Date: January 3, 1997 and March 26, 1997
Areas: Rate base, expenses and capital structure issues.

Union Electric Company
Case No. EO-96-14
Date: April 1999
Areas: Alternative Regulation Plan Agreements

Laclede Gas Company
Case No. GT-2001-329
Date: May 30, 2001
Areas: Gas Supply Incentive Plan

While in the employ of the Kansas State Corporation Commission in 1978, Mr. Schallenberg worked on a Gas Service Company rate case and rate cases of various electric cooperatives.