

Exhibit No.:
Issue: Revenue Requirement
Witness: Michael L. Brosch
Type of Exhibit: Surrebuttal Testimony
Sponsoring Party: Missouri Industrial Energy Consumers
Case No.: ER-2012-0166
Date Testimony Prepared: September 7, 2012

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

**In the Matter of Union Electric Company,
d/b/a Ameren Missouri's Tariff to Increase
Its Annual Revenues for Electric Service**

)
) **Case No. ER-2012-0166**
) Tariff No. YE-2012-0370
)
)

Surrebuttal Testimony of

Michael L. Brosch

Revenue Requirement

On behalf of

Missouri Industrial Energy Consumers

September 7, 2012

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**STATE OF MISSOURI
COUNTY OF JACKSON**

)
) **SS**
)

Affidavit of Michael L. Brosch

Michael L. Brosch, being first duly sworn, on his oath states:

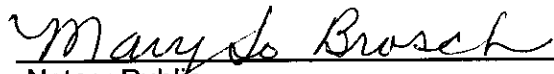
1. My name is Michael L. Brosch. I am President of Utilitech, Inc., having its principal place of business at PO Box 481934, Kansas City, Missouri 64148. Utilitech has been retained by the Missouri Industrial Energy Consumers in this proceeding on their behalf.
2. Attached hereto and made a part hereof for all purposes is my surrebuttal testimony which was prepared in written form for introduction into evidence in Missouri Public Service Commission Case No. ER-2012-0166.
3. I hereby swear and affirm that the testimony is true and correct and that it shows the matters and things it purports to show.



Michael L. Brosch

Subscribed and sworn to before me this 5th day of September 2012.





Notary Public

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Surrebuttal Testimony of Michael L. Brosch

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

2 A My name is Michael L. Brosch. My business address is PO Box 481934, Kansas
3 City, Missouri 64148.

4 **Q ARE YOU THE SAME MICHAEL L BROSCH WHO PREVIOUSLY SPONSORED**
5 **DIRECT TESTIMONY ON BEHALF OF THE MISSOURI INDUSTRIAL ENERGY**
6 **CONSUMERS ("MIEC")?**

7 A Yes. My qualifications were described in Appendix A to my direct testimony that was
8 previously submitted in this matter.

9 **Q WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?**

10 A My testimony is responsive to Ameren Missouri's rebuttal witnesses Ms. Barnes and
11 Mr. Reed who address the Company's proposal for non-traditional regulatory relief in
12 the form of special Plant-in-Service Accounting ("PISA"). My rebuttal testimony also
13 responds to Ameren Missouri witness James I. Warren regarding two income tax
14 related issues; the ratemaking treatment of Ameren's federal income tax deduction
15 for dividends paid on Ameren shares held in employee stock ownership plan
16 ("ESOP") accounts and rate base inclusion of accumulated deferred income taxes

1 ("ADIT") associated with the Company's investment in construction work in progress
2 ("CWIP") assets.

3 **Q ARE YOU PROPOSING ANY CHANGES TO THE RATE CASE ADJUSTMENTS**
4 **AND POSITIONS THAT WERE SET FORTH IN YOUR DIRECT TESTIMONY?**

5 A No. I continue to support the individual ratemaking adjustments that were
6 incorporated into the Schedules attached to my direct testimony. However, the
7 amounts associated with the CWIP-related ADIT issue will change in connection with
8 the true-up of ADIT balances.

9 **REGULATORY LAG**

10 **Q AT PAGE 19 OF HER REBUTTAL, MS. BARNES STATES, "EXCESSIVE**
11 **REGULATORY LAG HAS UNDOUBTEDLY HARMED THE COMPANY**
12 **SIGNIFICANTLY. IN THE PAST FEW YEARS THE COMPANY HAS**
13 **EXPERIENCED AN ENVIRONMENT WHERE COSTS ARE INCREASING AND**
14 **RETAIL LOAD HAS BEEN DECREASING, RESULTING IN MORE NEGATIVE**
15 **REGULATORY LAG WITH LIMITED OFFSETTING BENEFITS. THE FACT THAT**
16 **WE HAVE FILED FIVE RATE CASES IN JUST OVER FIVE AND ONE-HALF**
17 **YEARS DEMONSTRATES THIS FACT." SHOULD THE REGULATORY**
18 **FRAMEWORK IN MISSOURI BE CHANGED BECAUSE AMEREN MISSOURI'S**
19 **COSTS HAVE GROWN FASTER THAN REVENUES IN THE RECENT PAST?**

20 A No. To state the obvious, historical cost trends and financial results that were
21 experienced by Ameren Missouri and other Missouri utilities will not accurately predict
22 future outcomes. What is more important are future economic conditions and
23 financial outcomes, and utility management should be expected to carefully manage

1 costs going forward so as to optimize earnings. As noted in my direct testimony,
2 current levels of general inflation are relatively low, interest rates at which utilities can
3 finance rate base or refinance currently outstanding debt are at historically low levels,
4 technological improvements continue to drive productivity gains and management
5 should not be excused from the responsibility to control costs in this generally
6 favorable overall business environment.

7 **Q AT PAGE 19, MS. BARNES REFERENCES PROPOSITION 1 THAT WAS**
8 **ENACTED IN THE LATE 1970'S UNDER WHICH AN ELECTRIC UTILITY IS**
9 **PERMITTED TO RECOVER THE COST OF FACILITIES ONLY AFTER SUCH**
10 **FACILITIES ARE "FULLY OPERATIONAL AND USED FOR SERVICE." IS THE**
11 **COMPANY'S PROPOSED PISA MECHANISM REASONABLE BECAUSE OF**
12 **PROPOSITION 1 AND ITS PROHIBITION AGAINST INCLUDING CWIP IN RATE**
13 **BASE?**

14 **A** No. CWIP is permitted to earn a deferred return in the form of Allowance for Funds
15 Used During Construction ("AFUDC") when CWIP is not included in rate base. This
16 deferred return is fully compensatory because it accounts for the carrying costs
17 associated with the utility's investment in CWIP during the period of construction.
18 After construction is completed and the asset is transferred from CWIP to Plant in
19 Service, the AFUDC rules and the Proposition 1 prohibition no longer apply. An
20 entirely different set of accounting rules and ratemaking treatments apply to the new
21 asset after it is placed into service. It is for these completed construction projects
22 between rate cases that Ameren Missouri is now seeking modified accounting under
23 its PISA proposal.

1 **Q** **AT PAGE 20, MS. BARNES NOTES THAT HER CONCERN WITH TRADITIONAL**
2 **RATEMAKING IS ACTUALLY FOCUSED NOT UPON CWIP, BUT INSTEAD UPON**
3 **HOW TRADITIONAL REGULATION TREATS NEW ASSETS AFTER**
4 **CONSTRUCTION IS COMPLETED. SHE STATES, “THE FLAW IN THIS SCHEME**
5 **IS THAT THE UTILITY DOES NOT ACTUALLY RECOVER A RETURN ON ITS**
6 **INVESTMENT OR RECOVER THE DEPRECIATION EXPENSE ASSOCIATED**
7 **WITH THAT INVESTMENT UNTIL RATES ARE SET IN ITS NEXT RATE CASE,**
8 **MONTHS OR YEARS AFTER THE PLANT GOES INTO SERVICE. FOR THE**
9 **PERIOD OF TIME BETWEEN WHEN A FACILITY IS PLACED IN SERVICE AND**
10 **WHEN ITS COSTS ARE ULTIMATELY REFLECTED IN RATES, THE UTILITY**
11 **SUFFERS A PERMANENT LOSS OF THE RETURN AND DEPRECIATION**
12 **APPLICABLE TO THAT CAPITAL INVESTMENT FOR THAT PERIOD.” IS THERE**
13 **ANY “FLAW” IN THE REGULATORY TREATMENT OF NEWLY COMPLETED**
14 **PLANT- IN-SERVICE?**

15 **A** No. Ms. Barnes’ discussion is incomplete and is not indicative of any flaw. What
16 happens at completion of construction is actually more complex than what is
17 described by Ms. Barnes. If a newly constructed asset is replacing existing plant,
18 there is a corresponding retirement of an existing asset, which reduces both the Plant
19 in Service and the accumulated depreciation balances in the amount of the original
20 cost of the retired asset. Accumulated Depreciation is also charged with any costs
21 incurred to remove the old asset and is credited with any salvage received through
22 disposition of retired assets. As I noted in my direct testimony, a significant increase
23 to ADIT is a benefit created by new utility plant investment that must also be
24 recognized.

25 Important changes also occur within the utility’s income statement that are
26 ignored in Ms. Barnes’ rebuttal. For example, she states at page 20, “[t]he more that

an electric utility invests above the depreciation expense that is already built into rates, the greater the negative impact is on its financial performance.” This overly simplistic analysis fails to recognize many other income statement changes that can be initiated by the installation of new utility plant, including:

- Depreciation expense is eliminated on any assets that are retired whenever the new plant asset is replacing an existing plant asset.
- Maintenance expense may be reduced if newly installed assets are replacing deteriorated or unreliable facilities that have required unusually high maintenance activity and expense.
- Operating expenses may be reduced if the newly installed asset facilitates improved methods of operation or improves operational efficiency.
- Income tax deferrals are realized when newly constructed capital assets can be expensed as “repairs” for income tax purposes, improving cash flow and reducing rate base through the growth in ADIT.
- In the event new plant assets are associated with the connection of new customers or with the expansion of demand levels of existing customers, there are typically new revenues associated with such “growth” capital investments.

Q WHY DO YOU BELIEVE THERE IS NO “FLAW” IN THE TREATMENT OF NEWLY COMPLETED PLANT ADDITIONS UNDER TRADITIONAL TEST YEAR REGULATION?

A It is my view that traditional regulatory treatment of plant additions is more balanced and complete in recognizing all of the changes caused by utility construction and additions of new plant-in-service. Traditional test year regulation is the best and most widely employed method used to account for changes in plant-in-service because all of the impacts caused by newly installed plant assets are systematically updated, including all changes to the overall balances within plant-in-service, accumulated depreciation and ADIT within rate base, as well as levels of sales and revenues, operating and maintenance expenses and depreciation expenses that make up test

1 year operating income. The elegance of the traditional regulatory system is the
2 balanced approach to updating all of these variables within a matched and internally
3 consistent test year computation of the revenue requirement.

4 **Q AT PAGE 21, ACCORDING TO MS. BARNES, “THE SAME LOGIC THAT**
5 **SUPPORTED CONSTRUCTION ACCOUNTING FOR THE SIOUX SCRUBBERS**
6 **AND THE CALLAWAY NUCLEAR PLANT ALSO SUPPORTS THE ADOPTION OF**
7 **PLANT-IN-SERVICE ACCOUNTING FOR OTHER CAPITAL PROJECTS,**
8 **PARTICULARLY WHEN THE INDUSTRY AS A WHOLE, AND AMEREN**
9 **MISSOURI IN PARTICULAR, IS FACING A NEED TO REPLACE SIGNIFICANT**
10 **AMOUNTS OF AGING INFRASTRUCTURE AND SUBSTANTIAL**
11 **MODERNIZATION COSTS AND AT THE SAME TIME FACES FLAT OR EVEN**
12 **DECLINING LOAD GROWTH.” DO YOU AGREE?**

13 **A** No. The Commission allowed “construction accounting” for only discretely large and
14 unusual projects where the known circumstances of construction and expected
15 financial impacts of such projects merited exceptional accounting authority orders.
16 The Ameren Missouri PISA proposal is not limited to any particular projects and is not
17 supported by any specifically anticipated financial impacts. Instead, the Company
18 proposes an open-ended grant of accounting authority for all non-growth future
19 construction spending for the indefinite future. There is no similarity in either the
20 “logic” or the financial result achieved by prior Commission approvals of limited
21 construction accounting for discrete projects, when compared to Ameren Missouri’s
22 vastly expanded PISA proposal. The Company has made no showing of any inability
23 to finance the replacement of its aging infrastructure and has been in the process of
24 such replacement for many years. When costs have grown more rapidly than
25 revenues in the past, rate cases have been prosecuted to systematically update all

1 elements of the revenue requirement and this remedy remains available to Ameren
2 Missouri and other Missouri utilities in the future.

3 **Q DOES REGULATORY LAG CREATE AN IMPORTANT INCENTIVE FOR AMEREN**
4 **MISSOURI TO CAREFULLY MANAGE ITS CONSTRUCTION PROGRAM AND**
5 **THE LEVEL OF CAPITAL SPENDING?**

6 A Yes. Ms. Barnes rebuttal appears to admit that regulatory lag has an impact upon
7 management's spending habits, but she strikes a pejorative tone in stating,
8 "...historical regulatory policies are creating a disincentive for us to make investments
9 that would be beneficial if made, both to the Company's and customers' detriment."¹
10 On this point, the Commission should consider whether the public interest is best
11 served by encouraging more rapid investment in utility plant at ratepayers' expense
12 through approval of the PISA proposal and higher future prices to consumers, when
13 there has been no showing that existing regulatory policies are yielding inadequate
14 levels of utility investment or producing poor or deteriorating service quality.

15 **Q AMEREN MISSOURI'S WITNESS MR. REED ALSO WEIGHS IN ON THE**
16 **REGULATORY LAG DISCUSSION IN HIS REBUTTAL, STATING,**
17 **"SPECIFICALLY, MUCH OF THE EQUIPMENT INSTALLED BY AMEREN**
18 **MISSOURI DURING THE GROWTH YEARS FROM THE 1970S TO THE 1990S**
19 **NOW REQUIRES REPLACEMENT OR UPGRADING IN ORDER TO CONTINUE**
20 **TO PROVIDE SAFE AND RELIABLE SERVICE TO CUSTOMERS. FURTHER,**
21 **THE COMPANY IS MAKING CAPITAL INVESTMENTS IN ASSETS TO COMPLY**
22 **WITH LEGISLATIVE MANDATES, INCLUDING ENVIRONMENTAL AND**
23 **RENEWABLE ENERGY LAWS. ALL OF THESE INVESTMENTS ARE**

¹Rebuttal Testimony of Lynn M. Barnes, page 24, line 6.

1 **NECESSARY AND REQUIRE ADDITIONAL CAPITAL, BUT NONE CONTRIBUTE**
2 **TO REVENUE GROWTH FOR AMEREN MISSOURI. ABSENT MODIFICATIONS**
3 **TO THE REGULATORY FRAMEWORK IN MISSOURI, THE COMPANY WILL**
4 **CONTINUE TO SUFFER FROM REGULATORY LAG AND EARNINGS ATTRITION**
5 **AS A RESULT.”² HOW DO YOU RESPOND?**

6 A Like other electric utilities, Ameren Missouri continuously invests new capital to
7 replace and upgrade facilities. This is a necessary activity occurring in the normal
8 course of business in order to provide safe and adequate service, to comply with
9 legislative mandates and to continuously replace aging equipment. The continuous
10 addition of new plant-in-service is not a new or recent phenomenon. It is not
11 suddenly necessary to discard the traditional regulatory framework that carefully
12 balances the interests of customers and investors, in order to adopt new
13 comprehensive, and open-ended construction accounting in the form of Ameren
14 Missouri’s PISA proposal. Ameren Missouri’s PISA proposal does not address
15 regulatory lag at all, it merely selects one portion of Ameren Missouri revenue
16 requirement, the return on and depreciation of net plant additions, for continuous
17 regulatory asset accounting, while ignoring all the other changes in the Company’s
18 revenue requirement between test years. This will most certainly increase future
19 revenue requirements to the benefit of the utility and the detriment of its customers,
20 but PISA is not calibrated to produce any better measurement of the overall change
21 in revenue requirements between test years than simply filing a new rate case.

²Rebuttal Testimony of John J. Reed, page 14.

1 **PLANT-IN-SERVICE ACCOUNTING (“PISA”) PROPOSAL**

2 **Q MR. REED DISAGREES WITH YOUR VIEW THAT REGULATION IN MISSOURI IS**
3 **CONSISTENT WITH METHODS USED IN MANY STATES.³ HAS HE SHOWN**
4 **THAT PISA ACCOUNTING, AS RECOMMENDED BY AMEREN MISSOURI, HAS**
5 **BECOME A COMMON FEATURE OF UTILITY REGULATION TO COMBAT**
6 **REGULATORY LAG?**

7 **A No.** Mr. Reed claims to have provided “numerous examples of methods that other
8 states have used to reduce regulatory lag.” However, with regard to PISA in
9 particular, he cites only an Indiana ratemaking decision and a South Carolina order in
10 his rebuttal. He claims these two states have approved “post-in-service accounting”
11 in the form being proposed by Ameren Missouri.⁴

12 **Q DID THE INDIANA UTILITY REGULATORY COMMISSION (“IURC”) ADOPT A**
13 **FORM OF PISA ACCOUNTING SIMILAR OR ANALOGOUS TO WHAT IS BEING**
14 **PROPOSED BY AMEREN IN MISSOURI, AS STATED BY MR. REED?⁵**

15 **A No.** The IURC Final Order in Indiana Cause No. 43839 denied a proposed second
16 step rate increase for two specific capital projects, referred to as combustion turbine
17 “Dense Pack Projects” and instead authorized post-in-service AFUDC and deferred
18 depreciation for only these projects stating in its Final Order:

19 **B. Commission Findings.** We accept the position of the OUCC and
20 Industrial Group not to authorize a second step rate increase for
21 the Dense Pack Projects and instead authorize post-in-service
22 AFUDC and deferred depreciation as described by Vectren South
23 in its alternative rebuttal position. Given the fact that contracts
24 have already been executed, over \$8 million in capital
25 expenditures have already been made and the units are expected
26 to be in service within twelve months and 18 months of our Order

³Id.

⁴Id., pages 21-22.

⁵Id., page 21, lines 4-14.

1 in this Cause, we do not believe it is necessary or appropriate to
2 require the Company to make a separate accounting request at a
3 later time. We grant this request because of the earnings erosion
4 which would otherwise occur but also because of the significant
5 environmental and cost savings benefits that will immediately
6 accrue to the customers from these projects. Further, we note the
7 approved accounting treatment proposed by the company is
8 contingent upon a demonstration of at least 5% heat rate
9 improvement from each project. See Pet Ex. RGJ-RI, p. 20. We
10 find that the Company shall file a verified certification when each
11 project is completed and placed in service and report on the actual
12 improvements achieved by the projects. [IURC Final Order in
13 Cause No. 43839, 4/27/11, p.103]

14 What was approved in this Indiana rate case was not generalized post-in-service
15 continued construction accounting for overall plant additions, in the form being
16 proposed in Missouri by Ameren, as suggested in Mr. Reed's rebuttal testimony.
17 Indiana has a fuel adjustment clause that would flow to customers the fuel savings
18 benefits from the "at least 5% heat rate improvement from each project" that was
19 referenced in the Commission's Final Order. The fuel adjustment savings impacts
20 may have influenced the granting of post-in-service AFUDC and deferred
21 depreciation for the projects expected to create such fuel cost savings.

22 **Q DID THE PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA ADOPT A**
23 **FORM OF PISA ACCOUNTING SIMILAR TO WHAT IS BEING PROPOSED BY**
24 **AMEREN IN MISSOURI?**

25 **A** No. The "filing" described by Mr. Reed at page 22 of his rebuttal testimony makes
26 clear the scope of what was proposed by Duke Energy in South Carolina. This
27 proposal was limited to only "certain post-in-service costs" associated with two
28 specific capital investment programs, rather than the open-ended PISA proposal that
29 Ameren Missouri is seeking for an unlimited number of future construction projects.

1 **Q WAS MR. REED ABLE TO IDENTIFY ANY STATE COMMISSION IN HIS**
2 **REBUTTAL THAT HAS ACTUALLY APPROVED POST-IN-SERVICE**
3 **ACCOUNTING IN THE OPEN-ENDED FORM BEING PROPOSED BY THE**
4 **COMPANY IN MISSOURI?**

5 A No. The examples cited by Mr. Reed are limited scope examples of post-in-service
6 accounting for specific capital projects in only a few states (Indiana, South Carolina
7 and Missouri).

8 **Q DOES MR. REED DISPUTE YOUR OBSERVATION IN DIRECT TESTIMONY THAT**
9 **AMEREN MISSOURI'S RATE BASE IS EXPECTED TO GROW VERY LITTLE**
10 **BETWEEN 2012 AND 2016?**

11 A No. Instead, he implies that the lack of rate base growth is simply a function of
12 generally poor Missouri regulation and the absence of PISA. According to Mr. Reed,
13 "Mr. Brosch's observation is consistent with the assertion in my direct testimony that
14 because Ameren Missouri does not have a reasonable opportunity to earn its
15 authorized ROE, as evidenced by systemic and chronic under-earning since June
16 2007, the parent company (Ameren Corporation) has little incentive to invest in
17 Missouri beyond the basic requirements to maintain system reliability and service
18 quality."⁶

⁶Id., page 23.

1 **Q SHOULD THE COMMISSION APPROVE PISA IN AN EFFORT TO ENCOURAGE**
2 **AMEREN MISSOURI TO SPEND MORE ON FUTURE CAPITAL PROJECTS THAN**
3 **IS NECESSARY TO PROVIDE SAFE AND ADEQUATE SERVICE?**

4 **A**Of course not. Incremental capital spending by the utility often translates
5 directly into higher consumer rates in future rate cases. It is not clear whether
6 Mr. Reed is suggesting that PISA should be approved in order to encourage Ameren
7 Missouri to invest more than is necessary or prudent in Missouri. I believe it is clearly
8 the obligation of utility management to optimize its capital investment and to spend
9 only what is prudent and necessary to efficiently provide safe and adequate utility
10 services. If Ameren Missouri or Mr. Reed believes that the Company has not been
11 doing this under traditional regulation in Missouri, there is no clear statement of such
12 management failings within any of the Company's evidence in this proceeding. I
13 reject the premise that PISA is desirable simply as a tool to stimulate more capital
14 investment for construction projects that are only marginally needed to provide safe
15 and adequate utility service.

16 **Q AT PAGE 23, MR. REED STATES, "GIVEN MR. BROSCH'S VIEW REGARDING**
17 **THE ADEQUACY OF THE MISSOURI REGULATORY ENVIRONMENT, IT IS**
18 **UNCLEAR HOW HE EXPLAINS WHY AMEREN MISSOURI HAS NOT HAD A**
19 **REASONABLE OPPORTUNITY TO EARN ITS AUTHORIZED ROE ON A**
20 **WEATHER-NORMALIZED BASIS." HAVE YOU STATED THAT AMEREN**
21 **MISSOURI HAS NOT HAD A REASONABLE OPPORTUNITY TO EARN ITS**
22 **AUTHORIZED ROE?**

23 **A**I have not. It appears that Mr. Reed is confusing my position with his own. I
24 explained my conclusions regarding historical Ameren Missouri earnings and the

1 adequacy of the Company's opportunity to earn in my direct testimony. It seems to
2 be the Company's premise that historical Missouri earnings have been inadequate
3 and that all fault for Ameren Missouri's financial performance is properly directed
4 toward the regulation framework, rather than toward management performance.

5 **Q DOES MR. REED AGREE THAT IT IS POSSIBLE FOR A REGULATED ELECTRIC**
6 **UTILITY TO HAVE A REASONABLE OPPORTUNITY TO EARN ITS ALLOWED**
7 **RETURN AND STILL FAIL TO DO SO?**

8 A Yes, he does. Mr. Reed relied upon historical comparisons of the Company's earned
9 ROE compared to its authorized ROE to conclude that Ameren Missouri has not had
10 a reasonable opportunity to earn its authorized return. However, he did not conduct
11 any independent analysis regarding the quality of Ameren Missouri's management
12 and its decisions since June 2007.⁷ As I explained in my direct testimony, the
13 comparisons of actual earnings to authorized ROE levels prepared by Ameren
14 Missouri and relied upon by Mr. Reed were not prepared on a regulatory basis of
15 accounting and tend to understate achieved returns because of the inclusion of costs
16 not recoverable for ratemaking purposes.⁸

17 **Q DOES MR. REED IMPLY THAT AMEREN MISSOURI WILL COMPROMISE**
18 **SERVICE QUALITY IF THE PISA PROPOSAL IS NOT APPROVED?**

19 A His testimony on this point is less than clear. Mr. Reed states, "As noted earlier, the
20 fact that the Company had adjusted its expenditures in an effort to close the earnings
21 gap is not necessarily good for anyone, the Company or its customers, if the
22 consequence is that beneficial replacement of aging infrastructure or other service

⁷Ameren Missouri's response to MIEC 23.1, parts a through d.

⁸Direct Testimony of Michael L. Brosch, pages 12-14.

1 needs are under-funded. Mr. Brosch's clients may get a short-term "benefit" from
2 slightly lower rates, but his clients and customers generally are likely to suffer
3 intermediate and longer-term detriments."⁹ Mr. Reed has not demonstrated or
4 admitted any "under-funding" of Ameren Missouri's capital investment levels
5 historically, but seems to imply or threaten that customers "are likely to suffer" in the
6 future because Ameren Missouri may choose to neglect service quality if the PISA
7 proposal is not adopted.

8 **Q SHOULD AMEREN MISSOURI'S PISA PROPOSAL BE ADOPTED BECAUSE,**
9 **ACCORDING TO MR. REED, "...THE IMPACT ON CUSTOMER RATES WOULD**
10 **BE FAIRLY MINOR, GIVEN THAT THE SUMS WOULD BE CAPITALIZED WITH**
11 **THE RECOVERY TO OCCUR OVER THE LONG LIVES OF THE ASSETS WHICH**
12 **WERE PLACED IN-SERVICE"?¹⁰**

13 **A** No. All of the incremental charges to customers caused by recovery of the new
14 regulatory assets created by PISA would be additive to Ameren Missouri's
15 traditionally determined revenue requirement in future years. Excessive charges to
16 customers under the PISA proposal are not more acceptable simply because they
17 extend over many future periods.

18 **Q AT PAGE 24 OF HER REBUTTAL, MS. BARNES DISPUTES YOUR CRITICISM**
19 **THAT PISA FAILS TO ACCOUNT FOR ADIT GROWTH BETWEEN TEST YEARS,**
20 **STATING, "...ADIT WAS NOT TAKEN INTO ACCOUNT IN CALCULATING THE**
21 **ACCRUALS IN THE CONSTRUCTION ACCOUNTING FOR THE SIOUX**
22 **SCRUBBERS AND THE CALLAWAY NUCLEAR PLANT; HOWEVER, IT WAS**

⁹Id., page 23.

¹⁰Id., page 24.

TAKEN INTO ACCOUNT WHEN THE COSTS OF THOSE FACILITIES WERE INCLUDED IN RATES IN THE NEXT RATE CASE.” HOW DO YOU RESPOND?

A Ms. Barnes does not assert that accounting for ADIT changes as part of continued construction accounting is improper, but instead argues that it has not been done before. I would respond by noting that the limited instances where the Commission historically approved continued construction accounting, for the Sioux scrubbers and Callaway projects, there probably should have been more attention paid to ADIT impacts. I was not involved in those cases and cannot comment about the particulars of what circumstances were considered in specifying the scope of accounting authority that was granted. More importantly, Ameren Missouri is no longer satisfied with the narrower form of project-specific continued construction accounting that was granted historically by the Commission. It is disingenuous for the Company to now argue that the historically defined narrow accounting authority, that ignored ADIT effects, now defines precedent for the much broader PISA proposal being advocated.

The ADIT issue is much more important in the context of the unlimited scope of PISA accounting that would extend into the indefinite future and apply to the vast majority of future construction activities. The ADIT issue is also much more important today than historically because Ameren has changed its tax accounting methods to deduct currently as “repairs” expenses when the same costs are capitalized for book accounting purposes. If PISA is adopted, it must account for all of the cost of service impacts caused directly by new construction activity, including the substantial income tax deferral benefits recorded within ADIT.

ESOP INCOME TAX DEDUCTIONS

Q HAS AMEREN MISSOURI RESPONDED TO YOUR PROPOSAL TO RECOGNIZE THE INCOME TAX SAVINGS THE COMPANY REALIZES FROM PAYMENT OF DIVIDENDS ON AMEREN STOCK HELD IN ESOP ACCOUNTS?

A Yes. Ameren Missouri's rebuttal witness Mr. Warren does not dispute the existence of the ESOP deduction on Ameren consolidated tax returns or the recurring annual tax savings arising from the deduction, but instead argues that Ameren shareholders and not ratepayers should be the sole beneficiaries of the ESOP deduction. Mr. Warren argues that "...it is Ameren, and not UE or any other Ameren subsidiary, which pays the dividends with respect to 'applicable employer securities.' It is Ameren, therefore, that is entitled to the dividends paid tax deduction under the Code."¹¹

Q AT PAGE 6 OF HIS REBUTTAL, MR. WARREN ARGUES THAT, "UE DOES NOT PAY DIVIDENDS WITH RESPECT TO 'APPLICABLE EMPLOYER SECURITIES,' NOR HAS IT INCLUDED ANY SUCH DIVIDEND PAYMENTS IN ITS COST FOR SERVICE. FURTHER, IT HAS NOT CLAIMED A TAX DEDUCTION FOR DIVIDENDS PAID WITH RESPECT TO SUCH STOCK." DO THESE ARGUMENTS JUSTIFY ALLOWING THE DIVIDENDS PAID DEDUCTION ON THE AMEREN CONSOLIDATED INCOME TAX RETURN TO BENEFIT ONLY SHAREHOLDERS AND NOT RATEPAYERS?

A No. There are several problems with these arguments:

- First, Ameren Missouri, which is referred to as "UE" in Mr. Warren's rebuttal testimony, is allowed an authorized return on common equity for the purpose of compensating equity investors in Ameren Corporation who provide the invested equity capital in Ameren Missouri. It is disingenuous

¹¹Rebuttal Testimony of James I. Warren, page 5.

1 to suggest that the equity investors in Ameren Corporation, who are paid
2 dividends on common stock, are somehow distinct from the equity
3 investors who are compensated by Ameren Missouri ratepayers through
4 the authorized return on equity.

- 5 • Second, from a cash flow perspective, Ameren Missouri consistently pays
6 an upstream dividend to its parent Company, Ameren Corporation, which
7 cash is available to help fund the consistently declared and paid dividends
8 on Ameren Corporation's common stock.

- 9 • Third, the revenue requirement asserted by Ameren Missouri includes
10 significant costs that are allocated or attributed to the Company from other
11 Ameren affiliates and there is nothing wrong with equitably allocating or
12 attributing the tax deductions and credits "owned" by these affiliates
13 proportionately to Ameren Missouri, even though such deductions relate to
14 payments actually made by a different legal entity.

- 15 • Finally, if we rigidly applied the legal entity distinction between Ameren
16 Corporation and Ameren Missouri/UE that is advanced by Mr. Warren, we
17 are left with an absurd result through which the Commission could find that
18 Ameren Missouri/UE is not a taxpayer at all and owes no income taxes,
19 since Ameren Corporation actually files the returns and is liable for the
20 Company's income tax liability. Obviously, income tax expenses are
21 included within Ameren Missouri's revenue requirement because of the
22 fact that Ameren Corporation files a consolidated tax return that includes
23 Ameren Missouri's taxable revenues and deductible expenses.

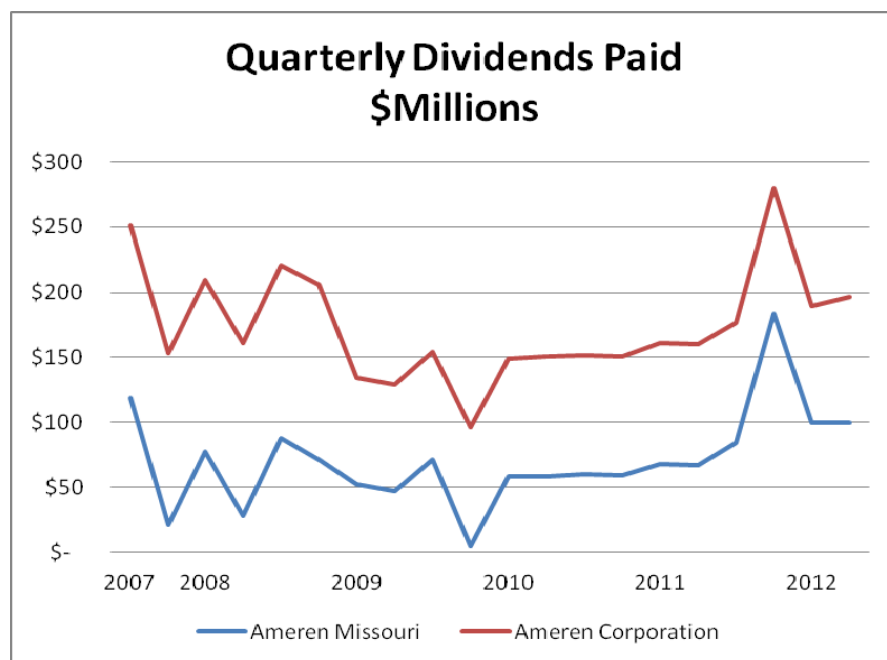
24 **Q SHOULD AMEREN MISSOURI RATEPAYERS BE DENIED AN ALLOCATED**
25 **SHARE OF THE AMEREN CORPORATION TAX DEDUCTION FOR DIVIDENDS**
26 **PAID ON ESOP SHARES BECAUSE AMEREN MISSOURI DOES NOT PAY**
27 **DIVIDENDS WITH RESPECT TO "APPLICABLE EMPLOYER SECURITIES" AS**
28 **SUGGESTED BY MR. WARREN?**

29 **A** No. It is not necessary for Ameren Missouri to directly pay a cost for its ratepayers to
30 be equitably allocated either the cost or the tax benefits arising from such payments.
31 As an example, when Ameren Services Company incurs expenses for shared service
32 activities that are allocated among Ameren Missouri, Ameren Illinois and the other
33 operating subsidiaries of Ameren Corporation, there is no dispute that associated tax
34 deductions are also proportionately allocated. The same principle should apply to

dividends, which are funded proportionately by Ameren Missouri and the other operating subsidiaries, even though they are actually paid by the parent company. Ameren Missouri includes in its asserted cost of service a return on equity capital that contemplates a dividend yield and growth component. As this equity return is actually collected through utility rates and accumulates within Ameren Missouri's retained earnings, it is periodically used to pay an upstream dividend to the parent that provides cash to support the payment of dividends to holders of Ameren Corporation's common stock.

Q HOW DO THE DIVIDENDS PAID BY AMEREN MISSOURI TO AMEREN CORPORATION COMPARE TO THE DIVIDENDS PAID BY AMEREN CORPORATION TO ITS SHAREHOLDERS IN RECENT YEARS?

A Ameren Missouri has consistently provided funding to support a significant share of the parent company's common stock cash dividends, as illustrated by this graph:



Source: Ameren Missouri's response to MIEC 23.8, Attachment 1

1 **Q AT PAGE 8 OF HIS REBUTTAL, MR. WARREN STATES, “ANY DIVIDEND PAID**
2 **BY AMEREN IS PAID AT THE SOLE DISCRETION OF AMEREN'S BOARD OF**
3 **DIRECTORS. THE BOARD'S DECISION IN THIS REGARD IS NOT LEGALLY**
4 **DEPENDENT ON ANYTHING THAT OCCURS AT UE. AMEREN HAS NUMEROUS**
5 **SOURCES OF FUNDS OUT OF WHICH IT CAN PAY DIVIDENDS. IT HAS OTHER**
6 **SUBSIDIARIES THAT PROVIDE CASH. BUT, IT IS NOT EVEN NECESSARY**
7 **THAT IT RECEIVE A SINGLE DOLLAR FROM ITS SUBSIDIARIES IN ORDER FOR**
8 **IT TO PAY DIVIDENDS. AMEREN COULD, IF IT WISHED, SIMPLY BORROW**
9 **ANY MONEY IT NEEDS TO PAY A DIVIDEND. IN OTHER WORDS, THE**
10 **DIVIDENDS PAID DEDUCTION CAN BE GENERATED WITH OR WITHOUT**
11 **DISTRIBUTIONS FROM UE.” DO THESE ARGUMENTS JUSTIFY ATTRIBUTING**
12 **THE ESOP DIVIDENDS TAX DEDUCTION SOLELY TO SHAREHOLDERS?**

13 **A No. These conceptual arguments do not change the reality of how Ameren actually**
14 **earns and pays its common dividends. The fact is that both Ameren Missouri and**
15 **Ameren Corporation pay dividends as a component of their overall return to common**
16 **equity investors. Purely as a result of the Company's selection of a holding company**
17 **corporate structure, the dividends that are publicly paid occur at the parent company**
18 **level. This distinction does not cause Ameren Missouri to request any lower**
19 **authorized return on common equity capital because it has no dividend expectations.**

20 Mr. Warren's assertion that Ameren's dividends paid on its publicly issued
21 common stock are “not legally dependent on anything that occurs at UE” is not
22 relevant to the issue of whether or not Ameren Missouri ratepayers are responsible
23 for providing a reasonable overall return on common equity capital, from which
24 discretionary dividends can be paid by Ameren Missouri and its parent/owner.
25 Dividends on common equity are inherently discretionary and are paid out of residual

1 earnings after all other costs are satisfied. Any notion of “legal dependency” is
2 inapplicable to such discretionary payments.

3 **Q IS THE FACT THAT DIVIDENDS ARE PAID OUT OF RETAINED EARNINGS OR**
4 **THAT RETAINED EARNINGS BELONG TO SHAREHOLDERS “VERY**
5 **SIGNIFICANT” AS SUGGESTED BY MR. WARREN?¹²**

6 A No. Legal ownership of retained earnings is not dispositive of ratemaking treatment.
7 Shareholders own the entire balance of equity capital in Ameren Missouri and this
8 balance is fully recognized in determining the capitalization balances and ratios used
9 for ratemaking purposes. Ownership distinctions do not preclude consideration of
10 dividend yields and market expectations for dividend growth when the Commission
11 determines a reasonable return on equity capital in setting rates for Ameren Missouri.
12 Ameren Missouri does not dispute attribution of a tax deduction for interest expenses
13 incurred by Ameren Missouri, even though the cash used to pay interest belongs to
14 Ameren and its shareholders. Ameren Missouri readily includes in its rate base all of
15 its jurisdictional Plant in Service, inventories and other assets, even though all of
16 these assets belong to and are “owned” by its shareholders rather than its ratepayers.
17 Ownership of retained earnings has nothing to do with equitable attribution of
18 dividend related tax deductions.

19 **Q IS AMEREN MISSOURI INCONSISTENT IN ITS OWN TREATMENT OF TAX**
20 **DEDUCTIONS ALLOWED ON DIVIDEND PAYMENTS?**

21 A Yes. A different federal income tax deduction is claimed by Ameren on its
22 consolidated return for dividends paid on certain UE preferred stock. This deduction
23 can be observed at Mr. Weiss’ workpaper GSW-WP-533 at the line captioned

¹²Id., page 8, lines 11-22.

1 “PREFERRED DIVIDEND DEDUCTION” and is fully attributed to ratepayers in
2 calculating test year income tax expense. Preferred dividends are declared and paid
3 out of retained earnings balances that belong to shareholders, just like ESOP
4 dividends on common stock, yet the Company has properly credited the tax
5 deduction benefits for these preferred dividend payments to ratepayers.

6 **Q ARE DIVIDENDS PAID ON AMEREN'S ESOP SHARES COMPARABLE TO**
7 **DISALLOWED CHARITABLE CONTRIBUTIONS, AS SUGGESTED BY MR.**
8 **WARREN?¹³**

9 A No. Mr. Warren has not identified any costs associated with Ameren's 401(k) plan or
10 its return on equity that have been “disallowed” by the Commission. Ameren's
11 shareholders have incurred no costs associated with the 401(k) plan that were
12 recorded below the line or otherwise not included in the Company's asserted revenue
13 requirement that might justify retention of the ESOP dividend tax deduction for the
14 sole benefit of shareholders. In response to MIEC Data Request 23.7, the Company
15 identified the following test year costs that were incurred in connection with the 401(k)
16 plan that contains the ESOP investment option:

<u>Cost Element</u>	<u>Amount</u>	<u>Disallowed?</u>
Compensation amounts paid to Ameren Missouri employees and contributed to the 401(k) plan	\$34,427,272	No
Compensation paid to affiliated companies' employees and contributed to the 401(k) plan	5,724,566	No
Ameren Missouri 401(k) Match expenses	13,062,987	No
401(k) Plan Administrative Expenses	77,315	Paid by Plan

¹³Id., page 9, lines 7-17.

1 I previously explained how the equity return allowed for Ameren Missouri in its
2 revenue requirement provides earnings and cash flow to support dividend payments.
3 There is no basis to conclude that the dividends paid on Ameren Corporation's stock
4 held in employees' retirement savings accounts represent costs that have ever been
5 disallowed by the Commission in determining rate levels in Missouri.

6 **Q AT PAGE 10, ACCORDING TO MR. WARREN, THE ESOP DIVIDEND TAX**
7 **DEDUCTION IS SUBJECT TO EMPLOYEE DISCRETION REGARDING 401(K)**
8 **INVESTMENT SELECTION AND THEREFORE THE DEDUCTION "...FLOWS**
9 **FROM THE WAY THEY CHOOSE TO INVEST THEIR EARNINGS AFTER THEY**
10 **ARE COMPENSATED. IN THIS WAY, TOO, THE TAX BENEFIT IS UNRELATED**
11 **TO THE CUSTOMERS' COST OF SERVICE. DOES THIS DISTINCTION JUSTIFY**
12 **ATTRIBUTING THE ESOP DIVIDEND TAX DEDUCTION BENEFIT TO**
13 **SHAREHOLDERS AND NOT RATEPAYERS?**

14 **A** No. The discretion exercised by employees has an impact upon the size of the tax
15 deduction, but not upon how the deduction should be treated for ratemaking
16 purposes. For example, if more employees elect to direct their 401(k) investments
17 into the ESOP, the dividends paid on such investments and the related tax deduction
18 amount would tend to increase. Mr. Warren has not disputed the amount of the
19 deduction that has been quantified for the test year or how that amount is allocated to
20 Ameren Missouri by the Staff and MIEC.

1 **Q AT PAGE 7 OF HIS REBUTTAL, MR. WARREN CLAIMS THAT THE DIRECT**
2 **COSTS OF ADMINISTERING THE ESOP ARE FUNDED BY THE PLAN ITSELF**
3 **AND THAT YOU INCORRECTLY ASSUMED THAT SUCH COSTS WERE BORNE**
4 **BY RATEPAYERS. IS THIS A REASON TO ATTRIBUTE THE ESOP TAX**
5 **DEDUCTION BENEFIT TO SHAREHOLDERS?**

6 **A No. My direct testimony stated, "...any administrative labor and expenses associated**
7 **with maintaining the ESOP plan are undoubtedly treated as jurisdictional operating**
8 **expenses when Ameren Missouri's revenue requirement is calculated." Even if**
9 **certain of Ameren's non-labor "direct costs" of administering the plan are charged to**
10 **plan participants, my point remains that Ameren Missouri has not shown that any**
11 **ESOP program expenses have been incurred by the Company and not been included**
12 **in its revenue requirement, so there is no basis to allow the Company to retain these**
13 **income tax savings as a windfall for shareholders. The table above confirms that**
14 **significant costs were incurred and included in the revenue requirement and that no**
15 **costs associated with this employee benefit program have been incurred by Ameren**
16 **Missouri and then recorded below the line or otherwise disallowed in setting rates.**

17 **Q MR. WARREN REFERS TO, "THE UNDERLYING PRINCIPLE, SOMETIMES**
18 **REFERRED TO AS THE 'BENEFITS FOLLOWS BURDENS' OR 'COST**
19 **RESPONSIBILITY' PRINCIPLE [THAT] , IS, IN MY EXPERIENCE UNIVERSAL IN**
20 **THE CASE OF SUCH EXPENDITURES."**¹⁴ **HOW WOULD THIS "PRINCIPLE"**
21 **INDICATE THAT THE ESOP DIVIDENDS INCOME TAX DEDUCTION SHOULD BE**
22 **ATTRIBUTED BETWEEN AMEREN SHAREHOLDERS VERSUS RATEPAYERS?**

23 **A All of the costs and burden incurred by the Company that are associated with the**
24 **Missouri share of Ameren's 401(k) benefit program have been treated as includable**

¹⁴Id., page 9, lines 15-17.

1 in determining the revenue requirement. Additionally, the Company has requested a
2 return on equity capital that is sufficient to support ongoing payment of common
3 dividends on the Missouri share of Ameren's common equity shares. With this factual
4 background, Mr. Warren relies upon arguments about employees' investment
5 discretion and who legally owns assets used to pay dividends, but he has failed to
6 identify any cost responsibilities or burdens that have been directly borne by Ameren
7 shareholders in connection with ESOP dividends. Therefore, I believe that a fair
8 application of the burden/benefit principle described by Mr. Warren would cause the
9 Missouri share of the ESOP dividend tax deduction benefit to be included in the
10 revenue requirement determination for the benefit of ratepayers.

11 **CWIP-RELATED ACCUMULATED DEFERRED INCOME TAXES**

12 **Q IN YOUR DIRECT TESTIMONY, YOU EXPLAINED A CHANGE BEING**
13 **PROPOSED BY THE COMPANY IN THE RATEMAKING TREATMENT OF**
14 **CERTAIN ADIT BALANCES THAT RELATE TO THE COMPANY'S CWIP ASSETS.**
15 **IS THIS ISSUE ADDRESSED BY ANY AMEREN MISSOURI WITNESSES?**

16 **A** None of the Company's witnesses had direct testimony on this proposed change in
17 ratemaking policy, but Mr. Warren sponsors rebuttal testimony explaining the basis
18 for the proposed change. According to Mr. Warren, "...the quantity of ADIT produced
19 by construction-related expenditures has increased markedly. Of particular note are
20 the expansion of the ability to deduct for Tax purposes certain indirect construction-
21 related overhead costs that are capitalized for Book purposes and, most dramatically,
22 the ability to characterize as deductible repairs for Tax purposes projects that are
23 treated as capital projects for Book purposes. The ADIT balances Mr. Brosch and I

1 address are those construction-related ADIT balances that are produced by
2 expenditures that, as of the end of the test period, remain in CWIP.”¹⁵

3 **Q ASIDE FROM THE ADIT AMOUNTS NOW BEING LARGER, WHAT RATIONALE**
4 **IS OFFERED BY MR. WARREN TO EXCLUDE CWIP-RELATED ADIT BALANCES**
5 **FROM RATE BASE?**

6 A According to Mr. Warren, the Company’s new position on this issue is based upon
7 several fairly fundamental arguments:

- 8 • The Company does not include its investment in CWIP in rate base.
9 Current customers therefore provide neither a return on, nor a return of,
10 that investment.
- 11 • Current customers are in no way burdened by CWIP investments.
- 12 • It is theoretically inappropriate to reduce the rates of current customers on
13 account of expenditures that will be entirely borne by a later “generation”
14 of ratepayers.
- 15 • The Company’s position is that current customers’ rates should be
16 precisely the same with or without CWIP.

17 The testimony that follows will respond to each of these arguments and will explain
18 why the existing regulatory practice with regard to CWIP-related ADIT balances
19 should not be changed.

20 **Q WHEN CWIP IS NOT INCLUDED IN RATE BASE, DOES THIS MEAN THAT**
21 **CURRENT CUSTOMERS PROVIDE NEITHER A RETURN ON NOR A RETURN OF**
22 **THAT INVESTMENT?**

23 A No. Current customers are providing an AFUDC return on CWIP investment that is
24 not included in rate base, which obligates current customers to pay higher rates in the
25 future rate cases after construction has been completed and each of the CWIP

¹⁵Id., pages 11-12.

1 projects is transferred into the Plant-in-Service accounts. This AFUDC return is a
2 non-cash return that is provided for within the FERC Uniform System of Accounts
3 (“USOA”) and has been treated as fully recoverable by this Commission when added
4 to the other costs incurred to acquire and construct new utility plant. Ameren Missouri
5 adds accrued amounts of AFUDC to its monthly earnings because of the assurance
6 that such amounts will be fully recoverable through the ratemaking process.

7 **Q HOW IMPORTANT IS AFUDC TO THE COMPANY’S EARNINGS?**

8 A AFUDC was accrued by Ameren Missouri in amounts that averaged \$3.8 million per
9 month throughout 2011 and to date in 2012.¹⁶ At these levels, AFUDC is an
10 important contributor to the Company’s overall financial performance.

11 **Q DOES MR. WARREN EXPLAIN WHAT IS MEANT BY THE REFERENCE IN HIS**
12 **REBUTTAL TESTIMONY TO “CURRENT” CUSTOMERS AND TO A “LATER**
13 **GENERATION OF RATEPAYERS”?**

14 A No. The distinctions being made by Mr. Warren with regard to CWIP could easily be
15 exaggerated if one improperly assumed that the population of Ameren Missouri’s
16 ratepayers currently being served will be significantly different in the Company’s next
17 rate case. While I have conducted no study of customer turnover in the Company’s
18 service territory, I expect based on my experience that most of the Company’s
19 “current” customers today will still be customers in the Company’s next Missouri rate
20 case. This is important because nearly all of the Company’s CWIP investment at the
21 end of the test year in the pending rate case will be in service and includable in rate
22 base in the next rate case.

¹⁶Based upon Ameren Missouri’s response to MIEC 23.11(d). See Brosch workpapers.

1 In response to MIEC Data Request 23.11, Mr. Warren stated, “My testimony
2 uses the term ‘current’ to refer to the customers that will be paying the rates that have
3 been established without regard to the current CWIP balance. While I have no
4 specific knowledge regarding changes in the composition of Ameren Missouri’s
5 customer base over time, as a general matter I believes [sic] that it changes
6 constantly, although a large core of the same customers likely remains over time.”

7 **Q ARE CURRENT CUSTOMER BURDENED BY CWIP?**

8 A Yes. They are burdened with the responsibility to pay higher returns and depreciation
9 expense to fully repay the accrued AFUDC balances on today’s CWIP investment.
10 Nearly all of these AFUDC amounts will become payable in the Company’s very next
11 rate case because all of Ameren Missouri’s CWIP projects that were active at July 31,
12 2012 are estimated to be in service on or before July 31, 2013.¹⁷ The CWIP-related
13 ADIT balances Mr. Warren seeks to keep solely for shareholder benefit are not
14 properly saved for a “later generation of ratepayers” as he suggests, but relate to
15 construction activity that is short-term in nature and expected to be completed within
16 the year.

17 **Q DOES MR. WARREN COMPLETELY DISCOUNT THE VALUE OF THE AFUDC**
18 **RETURN THAT AMEREN MISSOURI IS ALLOWED TO EARN ON ITS CURRENT**
19 **INVESTMENT IN CWIP?**

20 A It appears that he does. He complains that AFUDC earned on CWIP is not a “cash
21 return to the company during construction.” He states “AFUDC is an accounting entry
22 that increases non-cash income during the construction period of the asset. This

¹⁷Ameren Missouri’s response to MIEC 23.13, attachment listing CWIP projects and estimated completion dates.

1 entry has no effect on revenue requirement during the construction period and does
2 not result in a cash return on or the return of the CWIP investment during
3 construction.”¹⁸

4 **Q DOES THE DISTINCTION BETWEEN AFUDC AS A NON-CASH RETURN**
5 **VERSUS A CASH RETURN MAKE IT ANY LESS VALUABLE ON AMEREN**
6 **MISSOURI'S INCOME STATEMENT?**

7 A No. AFUDC accruals contribute to income in the same manner as all other
8 accounting entries that impact revenues and expenses. When it comes to Ameren
9 Missouri's new PISA proposal, there seems to be a strong appetite for additional
10 non-cash earnings in the form of continuing construction accounting for plant added
11 between test years. It is highly inconsistent for Ameren Missouri to disparage the
12 quality of AFUDC earnings in its efforts to deny ratepayers the benefits of
13 CWIP-related ADIT balances at the same time the Company advocates for more
14 non-cash PISA earnings to improve its overall financial performance, all at ratepayers'
15 expense.

16 **Q WHAT IS THE SIGNIFICANCE OF AFUDC TO MR. WARREN'S PROPOSAL TO**
17 **EXCLUDE CWIP-RELATED ADIT IN DETERMINING RATE BASE?**

18 A According to Mr. Warren, the Company can only begin to earn a cash return on its
19 CWIP investment “When the construction of the project is complete and the asset is
20 Plant in Service....It is only at this time, when rate are adjusted to reflect the plant that
21 has been placed in service (and not before), that the ADIT related to Plant in Service'
22 book and tax basis differences should also be included in rate base as a liability that

¹⁸Rebuttal Testimony of James I. Warren, page 14.

1 offsets rate base.”¹⁹ Mr. Warren appears to place great importance upon the delay in
2 charging customers a “cash” return on CWIP while assigning little value to the
3 continuous accrual of an AFUDC return that occurs throughout the construction
4 period.

5 **Q IS THE AFUDC RETURN ALLOWED UNDER FERC REGULATION AND BY THE**
6 **MISSOURI COMMISSION INADEQUATE IN ITS TREATMENT OF CWIP**
7 **INVESTMENTS MADE BY AMEREN MISSOURI AND OTHER PUBLIC UTILITIES?**

8 A No. AFUDC returns are based upon the Company’s actual cost of capital and fully
9 compensate for the return requirement during the construction period. The recorded
10 amounts of AFUDC are added into the balances of Plant in Service that are
11 includable in rate base and are then subject to recovery from customers over the life
12 of the constructed new plant. When asked, Mr. Warren stated that “My testimony
13 does not assert that there is any deficiency in the Company’s AFUDC recordation.”

14 **Q IN YOUR DIRECT TESTIMONY, YOU EXPLAINED THAT THE COMPANY’S**
15 **CWIP-RELATED ADIT BALANCES MUST CONTINUE TO BE INCLUDED IN RATE**
16 **BASE OR ELSE AMEREN MISSOURI’S AFUDC ACCOUNTING WILL BE**
17 **EXCESSIVE BECAUSE THE AFUDC CALCULATIONS APPLY A CARRYING**
18 **CHARGE RATE TO THE GROSS INVESTMENT IN SUCH CONSTRUCTION WITH**
19 **NO ACCOUNTING FOR CWIP-RELATED ADIT BENEFITS THAT TEND TO**
20 **REDUCE SUCH INVESTMENT”²⁰ DOES MR. WARREN DISPUTE THIS POINT?**

21 A No. Mr. Warren is focusing upon the timing of cash flows in his rebuttal testimony,
22 without regard to the problems of AFUDC over-recovery his omission of CWIP-related

¹⁹Id., page 14.

²⁰Direct Testimony of Michael L. Brosch, page 36.

1 ADIT balances would cause. He is concerned that under the existing accounting for
2 CWIP-related ADIT balances, “Customer rates today would be reduced on account of
3 expenditures which they have not yet funded and which they do not yet support (*i.e.*,
4 which are not reflected in the rate base which was used to set their rates). This rate
5 reduction would serve to reduce the Company’s current cash flow precisely at a time
6 when the funds are most in need – when it is investing in the assets under
7 construction. To me, this makes little sense.”²¹

8 **Q DID YOU ASK THE COMPANY TO EXPLAIN THE MODIFICATIONS TO ITS**
9 **AFUDC ACCRUAL PROCEDURES THAT WOULD BE IMPLEMENTED TO**
10 **PREVENT OVER-RECOVERIES OF AFUDC IF THE COMPANY’S NEW POSITION**
11 **TO EXCLUDE CWIP-RELATED ADIT BALANCES FROM RATE BASE IS**
12 **ADOPTED BY THE COMMISSION?**

13 **A** Yes. This question was asked in MIEC Data Request 23.16. In its response, Ameren
14 Missouri stated, “The Company does not propose to alter its AFUDC accrual
15 procedures. The ADIT associated with costs included in CWIP will impact rates when
16 it is reflected in ratemaking in the first rate proceeding in which the associated assets
17 are reflected in rate base.”

18 **Q IF THE COMPANY’S AFUDC PROCEDURES REMAIN UNCHANGED AND**
19 **CWIP-RELATED ADIT BALANCES ARE NO LONGER INCLUDED IN RATE BASE,**
20 **WILL CUSTOMERS BE OVERCHARGED?**

21 **A** Yes. If CWIP-related ADIT balances are no longer included in rate base, it is
22 essential that AFUDC procedures be modified to prevent excessive capitalization of
23 AFUDC, for the reasons explained and quantified with example calculations in my

²¹Rebuttal Testimony of James I. Warren, page 15

1 direct testimony.²² The Company's failure to address this problem is a serious
2 omission that cannot be ignored.

3 **Q WILL CONTINUATION OF THE EXISTING POLICY OF INCLUDING**
4 **CWIP-RELATED ADIT BALANCES IN RATE BASE RESULT IN "...REDUC[ING]**
5 **THE COMPANY'S CURRENT CASH FLOW PRECISELY AT A TIME WHEN THE**
6 **FUNDS ARE MOST IN NEED – WHEN IT IS INVESTING IN THE ASSETS UNDER**
7 **CONSTRUCTION,"²³ AS ALLEGED BY MR. WARREN?**

8 A No. It should be understood that what has changed is Ameren Missouri's tax
9 deferrals that have vastly increased the Company's overall ADIT balances through a
10 combination of bonus depreciation deductions affecting plant-in-service and the
11 "repairs" deduction change mentioned at page 12 of Mr. Warren's testimony that
12 impacts CWIP-related ADIT balances. These changes have greatly increased the
13 Company's current cash flows by the complete avoidance of currently payable
14 income taxes. The Company's proposal to change the accounting for CWIP-related
15 ADIT balances is more about keeping for shareholders more of the large, new tax
16 deferral benefits than about "reducing cash flow" as suggested by Mr. Warren.

17 **Q HAVE THE VASTLY EXPANDED INCOME TAX DEFERRALS ARISING FROM**
18 **THE REPAIRS DEDUCTION FOR COSTS THAT ARE CAPITALIZED ON THE**
19 **BOOKS CAUSED AMEREN MISSOURI TO ALSO SEEK EXCLUSION OF**
20 **CWIP-RELATED ADIT BALANCES IN ILLINOIS RATE CASES?**

21 A No. Even though the magnitude of income tax deferrals in Illinois have expanded
22 proportionately, the Ameren Illinois Companies continue to include CWIP-related

²²Direct Testimony of Michael L. Brosch, pages 37-38.

²³Rebuttal Testimony of James I. Warren, page 15.

1 ADIT balances in rate base, as noted in my direct testimony. I encourage the
2 Commission to reject Ameren Missouri's proposed changes regarding CWIP-related
3 ADIT for all the reasons set forth in my direct and surrebuttal testimony.

4 **Q AT PAGE 12, MR. WARREN ALSO STATES, "THE COMPANY'S POSITION IS**
5 **THAT CURRENT CUSTOMERS' RATES SHOULD BE PRECISELY THE SAME**
6 **WITH OR WITHOUT CWIP." IS THIS A REASONABLE GOAL?**

7 A No. This has never been a reasonable goal. At page 12 of his rebuttal testimony, Mr.
8 Warren explains his position, stating, "The Company's filing in this case reflects its
9 position that it is theoretically inappropriate to reduce the rates of current customers
10 on account of expenditures that will be entirely borne by a later "generation" of
11 ratepayers." I submit that full recognition of CWIP-related ADIT in rate base is
12 essential to account for these tax deferral benefits. Mr. Warren's approach would
13 cause the benefits to be improperly retained for shareholders. Under Mr. Warren's
14 approach, rate base would be overstated now by ignoring CWIP-related ADIT and
15 rate base would be overstated again in the future because the FERC rules governing
16 AFUDC calculations allow a full return on CWIP balances that have not been reduced
17 by ADIT. The tax deferral benefits arise from constructing new assets allows Ameren
18 Missouri to defer the payment of income taxes and shareholders should not be
19 allowed to retain these benefits simply because the CWIP returns earned by the
20 Company are in the form of AFUDC.

21 **Q DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?**

22 A Yes.