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MISSOURI PUBLIC SERVICE COMMISSION

CASE NO. ER-2012-0166

REBUTTAL TESTIMONY

OF

JOHN J. REED

ON

BEHALF OF

**UNION ELECTRIC COMPANY
d/b/a Ameren Missouri**

**St. Louis, Missouri
August, 2012**

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1 **REBUTTAL TESTIMONY OF JOHN J. REED**
2 **CASE NO. ER-2012-0166**

3 **I. INTRODUCTION**

4 **Q. PLEASE STATE YOUR NAME AND EMPLOYMENT POSITION.**

5 A. My name is John J. Reed, and I am Chairman and Chief Executive Officer of
6 Concentric Energy Advisors, Inc. and CE Capital Advisors, Inc. (together
7 “Concentric”).

8 **Q. HAVE YOU PREVIOUSLY FILED DIRECT TESTIMONY IN THIS**
9 **PROCEEDING?**

10 A. Yes, I filed Direct Testimony on behalf of Union Electric Company d/b/a Ameren
11 Missouri (“Ameren Missouri” or the “Company”).

12 **Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS**
13 **PROCEEDING?**

14 A. The purpose of my rebuttal testimony is to respond to the direct testimony of
15 Mr. Michael P. Gorman and Mr. Michael L. Brosch on behalf of the Missouri
16 Industrial Energy Consumers (“MIEC”) as it relates to regulatory lag and earnings
17 attrition.

18 **II. SUMMARY OF KEY CONCLUSIONS**

19 **Q. WHAT ARE YOUR KEY CONCLUSIONS?**

20 A. My key conclusions are:

- 1 • Ameren Missouri has not had a reasonable opportunity to earn its allowed return
2 for years. The Company has, with only very limited exceptions, been unable to
3 earn its allowed return on a weather-normalized basis since June 2007.
- 4 • Ameren Missouri's rates are out-of-date the moment they become effective and,
5 as a result, the Company is forever denied the opportunity to recover costs it
6 incurs to serve its customers. Absent modifications to the regulatory framework
7 in Missouri, the Company will continue to suffer from regulatory lag and earnings
8 attrition.
- 9 • Other jurisdictions have approved regulatory mechanisms that are analogous to
10 Ameren Missouri's Plant-in-Service Accounting proposal, and have noted that
11 such mechanisms reduce earnings attrition and benefit customers. In addition, the
12 Commission has previously approved "construction accounting" treatment for
13 major construction projects in Missouri.
- 14 • The Commission's adoption of the Plant-in-Service Accounting treatment and the
15 proposed two-way storm restoration cost tracker will provide Ameren Missouri
16 with a more reasonable opportunity to earn its authorized ROE and ultimately will
17 benefit the Company's customers through a more reliable electric system at rates
18 that remain among the lowest in the nation.
- 19 • I continue to recommend strongly that the Commission approve the Company's
20 proposed Plant-in-Service Accounting treatment and storm cost tracker and
21 continue the Company's existing rider and tracking mechanisms, as well as the
22 revised 10.50% ROE recommendation of Company witness Hevert.

1 **III. RESPONSE TO MISSOURI INDUSTRIAL ENERGY CONSUMERS**

2 *GENERAL OBSERVATIONS*

3 **Q. PLEASE SUMMARIZE MR. GORMAN'S POSITION AS IT RELATES TO**
4 **REGULATORY LAG AND EARNINGS ATTRITION FOR AMEREN**
5 **MISSOURI.**

6 A. Mr. Gorman states that the Missouri regulatory environment is balanced and supports
7 the development of just and reasonable rates that provide a reasonable opportunity for
8 Ameren Missouri to earn its authorized return on equity.¹ In support of his position,
9 Mr. Gorman observes that credit rating analysts have noted that, over the last several
10 rate cases, Ameren Missouri's rate decisions have been constructive and credit
11 supportive.² Further, Mr. Gorman contends that the Company's critique of regulatory
12 mechanisms is not designed to strike a fair balance between investors and ratepayers.³
13 Mr. Gorman contends that Ameren Missouri failed to consider the proposed impact of
14 changes to the Missouri regulatory framework on the competitiveness, predictability
15 and stability of utility rates.⁴ For these reasons, Mr. Gorman recommends that the
16 Commission reject Ameren Missouri's proposed regulatory mechanisms.⁵

1 See direct testimony and schedules of Michael P. Gorman, at 3.

2 Ibid.

3 Ibid.

4 Ibid., at 66-67.

5 Ibid., at 3.

1 **Q. DO YOU AGREE WITH MR. GORMAN THAT THE REGULATORY**
2 **ENVIRONMENT IN MISSOURI PROVIDES THE COMPANY WITH A**
3 **REASONABLE OPPORTUNITY TO EARN ITS AUTHORIZED ROE?**

4 A. No, I do not. While the Commission has allowed Ameren Missouri to implement
5 certain cost tracking mechanisms, such as a Fuel Adjustment Clause, a pension cost
6 tracking mechanism, and a vegetation and infrastructure management tracker, among
7 others, the Company has not had a reasonable opportunity to earn its authorized
8 return on a weather normalized basis since June 2007. This provides clear,
9 quantitative evidence that Ameren Missouri has been unable, with only limited
10 exceptions, to consistently earn its authorized ROE since June 2007, despite filing
11 multiple rate cases during this period. A principal reason for this chronic earnings
12 attrition is the Company's non-revenue producing capital investments. As such,
13 Ameren Missouri's proposed cost recovery mechanism relating to Plant-in-Service
14 Accounting would address one of the key issues that has prevented the Company
15 from having a reasonable opportunity to earn its authorized ROE, and adoption of a
16 two-way storm restoration cost tracker would fairly address volatile and unpredictable
17 storm costs while not creating a situation where the Company could lose money if it
18 continues its aggressive storm response efforts.

1 **Q. MR. GORMAN STATES THAT REGULATORY MECHANISMS SHOULD**
2 **BALANCE CUSTOMERS' NEED FOR COMPETITIVE AND**
3 **PREDICTABLE RATES WITH AMEREN MISSOURI'S NEED TO**
4 **RECOVER REASONABLE AND PRUDENT COSTS. DO YOU AGREE**
5 **THAT THIS IS THE APPROPRIATE STANDARD?**

6 **A.** No. I disagree with Mr. Gorman that the appropriate standard for review is whether a
7 regulatory mechanism results in "competitive and predictable" rates for customers.
8 The traditional standard for setting utility rates is "just and reasonable." As explained
9 in my direct testimony, under the regulatory compact, each participant in the
10 regulatory relationship has certain interrelated responsibilities, the satisfaction of
11 which is critical for the regulated utility industry to function effectively and for its
12 customers to benefit from safe and reliable service.⁶ Regulatory mechanisms are one
13 tool that utility regulators have used to enable a utility to recover its reasonable and
14 prudent costs so that the utility has a better opportunity to earn its authorized return.

15 While I understand customers' desire for competitive and predictable rates,
16 the Commission has an obligation to ensure that Ameren Missouri has a reasonable
17 opportunity to recover its prudently-incurred costs, including capital costs, through
18 customer rates. While utility regulators often consider the affordability and
19 predictability of customer rates and attempt to avoid rate shock for customers
20 whenever possible, the Commission's ultimate responsibility is to approve just and
21 reasonable rates, which includes the requirement that a utility be provided with a
22 reasonable opportunity to earn a fair return.

⁶ See direct testimony of John J. Reed, at 10.

1 **Q. MR. GORMAN CONTENDS THAT AMEREN MISSOURI DID NOT**
2 **BELIEVE THE IMPACT ON RATEPAYERS OF ITS PROPOSED**
3 **REGULATORY MECHANISMS WAS A SIGNIFICANT CONSIDERATION.**
4 **DO YOU AGREE WITH MR. GORMAN'S PERSPECTIVE?**

5 A. No, I do not. On several occasions in my direct testimony, I explain the effect of
6 regulatory lag and earnings attrition on customers, as well as the impact on customers
7 of implementing regulatory mechanisms to mitigate those effects. Specifically, with
8 regard to Ameren Missouri's proposed Plant-in-Service Accounting and the two-way
9 storm restoration cost tracker, both mechanisms will provide regulatory efficiencies
10 that ultimately benefit customers through (1) a reduced cost of service, and
11 (2) helping to reduce pressure to limit or reduce investments in the Company's
12 system. These measures ultimately will benefit the Company's customers through a
13 more reliable electric system at rates that remain among the lowest in the nation.

14 **Q. DO YOU AGREE WITH MR. GORMAN THAT THE COMPANY'S**
15 **PROPOSED REGULATORY MECHANISMS SHOULD BE CONSIDERED**
16 **EXTRAORDINARY, AND SHOULD BE REJECTED BECAUSE THEY FAIL**
17 **TO STRIKE A FAIR BALANCE BETWEEN INVESTORS AND**
18 **RATEPAYERS?**

19 A. No, I do not. Ameren Missouri's proposed Plant-in-Service Accounting and two-way
20 storm cost tracker are designed to address the chronic earnings attrition for the
21 Company since June 2007 and to help promote a reasonable opportunity for the
22 Company to earn a fair return. These are certainly not extraordinary mechanisms, as
23 Mr. Gorman has characterized them. Rather, the Company's proposed regulatory

1 mechanisms are consistent with policies that have been adopted in other jurisdictions.
2 In addition, these proposed regulatory mechanisms will benefit customers by
3 providing Ameren Missouri the necessary incentive to continue to invest in its system
4 so that customers continue to enjoy reliable service at affordable rates. As discussed
5 in my direct testimony, the regulatory compact provides that Ameren Missouri has an
6 obligation to provide safe, adequate and reliable service at reasonable rates, and in
7 return the Commission is expected to provide a regulatory environment that allows
8 the Company to recover its prudent costs on a timely basis and to compensate
9 investors for placing their capital at risk.⁷

10 **Q. DO YOU AGREE WITH MR. GORMAN THAT AMEREN MISSOURI'S**
11 **PROPOSED REGULATORY MECHANISMS TILT THE BALANCE OF THE**
12 **REGULATORY PROCESS IN FAVOR OF INVESTORS, AND SHIFT RISK**
13 **FROM INVESTORS TO CUSTOMERS?**

14 A. No, I do not. As discussed throughout my direct and rebuttal testimony, under the
15 current regulatory framework in Missouri, the Company has not had a reasonable
16 opportunity to earn its authorized ROE on a weather normalized basis since June
17 2007. The proposed Plant-in-Service Accounting and the two-way storm cost
18 restoration tracker are modest steps that the Commission can take to provide Ameren
19 Missouri with a better opportunity to earn its authorized ROE. Mr. Gorman seems to
20 suggest that Ameren Missouri and its investors should never expect to actually earn
21 the return authorized by the Commission. However, the ROE awarded by the
22 Commission represents what it considers to be the "cost" of equity and is "just and

⁷ Ibid, at 10-11.

1 reasonable.” Ameren Missouri’s proposed regulatory mechanisms are not intended to
2 shift risk from investors to customers, as Mr. Gorman states, but rather to provide the
3 Company with a reasonable opportunity to cover its cost of equity, which requires
4 that it earn the return that the Commission has determined is appropriate.

5 ***CALCULATION OF EARNED RETURNS***

6 **Q. DO YOU AGREE WITH MR. BROSCHE THAT IN ORDER TO**
7 **REASONABLY ASSESS WHETHER AMEREN MISSOURI HAS BEEN**
8 **ABLE TO EARN ITS AUTHORIZED RETURN, THE COMPANY SHOULD**
9 **HAVE CALCULATED ITS EARNED RETURNS BASED ON REGULATORY**
10 **ADJUSTMENTS APPROVED BY THE COMMISSION RATHER THAN ON**
11 **ACCOUNTING RETURNS?⁸**

12 A. No, I do not. As explained in the rebuttal testimony of Company witness Weiss, the
13 Company’s ROE calculations were originally prepared using the monthly and/or
14 quarterly reports filed by the Company with the Commission and do not reflect any of
15 the adjustments. From my perspective, the earned return calculations presented in
16 Ameren Missouri’s direct testimony are reasonable and appropriate because they
17 represent the actual return an investor would receive on its investment, and are
18 consistent with the figures reported to the Commission. While investors understand
19 that certain adjustments are made by regulators, the relevant return to an investor is
20 the actual net income that Ameren Missouri is able to earn on its investment in rate
21 base. When investors are establishing return expectations, they do so based on the
22 probability that Ameren Missouri will successfully earn a certain percentage on its

⁸ See direct testimony of Michael L. Brosch, at 13.

1 invested capital on a reasonably consistent basis. They pay much less attention to
2 isolated regulatory adjustments that may on a one-time basis lower, or raise, earnings.
3 And if one is going to look at adjusted returns similar to the way suggested by Mr.
4 Brosch, one must consider how those returns look over time and whether the
5 regulatory policies being employed provide a reasonable opportunity to earn fair
6 returns over time. The data tell us that this reasonable opportunity has not existed and
7 will not exist absent changes to the regulatory policies historically employed in
8 Missouri.

9 **Q. WHAT IS YOUR RESPONSE TO MR. BROSCH'S OBSERVATION THAT**
10 **AMEREN MISSOURI'S OWN CALCULATIONS SHOW A "REMARKABLY**
11 **STABLE STREAM OF EARNINGS THROUGHOUT THE MAJOR**
12 **ECONOMIC SLOWDOWN, INDICATING THE OVERALL**
13 **EFFECTIVENESS OF THE REGULATORY APPROACH IN MISSOURI"?⁹**

14 **A.** I disagree with Mr. Brosch's characterization of the stability of Ameren Missouri's
15 earnings during the economic slowdown. The relevant question is not whether
16 Ameren Missouri's earnings have been "stable" during the recent recession, but
17 whether those earnings have been adequate as compared to the Company's authorized
18 return. An actual return of five percent each year would indicate that Ameren
19 Missouri's earnings were stable, but it would not indicate that the Company's
20 earnings were sufficient to compensate investors for the risks associated with
21 investing in the Company's common equity.

⁹ Ibid, at 16.

1 **Q. PLEASE SUMMARIZE MR. BROSCH'S POSITION WITH REGARD TO**
2 **FUTURE EARNINGS ATTRITION FOR AMEREN MISSOURI.**

3 A. According to Mr. Brosch, the Company has not demonstrated that future earnings will
4 continue to suffer from attrition.¹⁰ Furthermore, Mr. Brosch states that "recent and
5 projected financial information suggests an improving trend in earnings and costs and
6 Ameren Missouri's favorable position arising from its significant Net Operating Loss
7 carry-forward position will allow the Company to avoid the payment of income taxes
8 for several years."¹¹ Finally, Mr. Brosch claims that Ameren Missouri has failed to
9 "demonstrate either a credible expectation of future earnings attrition or any showing
10 that the proposed PISA [Plant-In-Service Accounting] or storm cost tracker
11 accounting are appropriately calibrated to address such quantified attrition."¹²

12 **Q. WHAT IS YOUR RESPONSE TO MR. BROSCH ON THESE ISSUES?**

13 A. To the extent that Ameren Missouri continues to make non-revenue producing
14 capital investments to replace aging infrastructure and comply with environmental
15 requirements, and to the extent that the Company continues to experience severe
16 storms which require immediate and costly service restoration efforts, Ameren
17 Missouri's future earnings will continue to fall short of the Company's authorized
18 ROE unless the regulatory environment in Missouri changes to allow Ameren
19 Missouri to recover prudently incurred costs on a more timely basis. These items
20 don't even account for other cost increases, or for the fact that load growth, which in
21 decades past tended to help utilities offset cost increases, has become flat or in some

¹⁰ Ibid, at 10-11.

¹¹ Ibid, at 10.

¹² Ibid.

1 cases is declining. There is simply no basis for Mr. Brosch's conclusion that the
2 earnings situation at Ameren Missouri will suddenly change in the future if the
3 regulatory environment continues to permit excessive regulatory lag and earnings
4 attrition rather than providing a reasonable opportunity for the Company to earn its
5 authorized ROE. Even if a utility, including Ameren Missouri, can temporarily
6 mitigate the impact of a regulatory environment that has not provided a reasonable
7 opportunity to earn a fair return by severe cost-cutting measures, such cost-cutting is
8 not sustainable in the intermediate or longer-terms because it will likely cause the
9 utility to under-invest in its system and in its operations, inevitably leading to
10 reductions in the quality of its service and, ultimately, higher costs.

11 **Q. PLEASE SUMMARIZE MR. BROSCH'S POSITION AS IT RELATES TO**
12 **MANAGEMENT'S RESPONSIBILITY FOR CONTROLLING COSTS.**

13 A. Mr. Brosch states that in evaluating earned returns of public utilities, it is not
14 reasonable to excuse company management from its responsibility for controlling
15 costs and maximizing operational efficiencies.¹³ He also observes that an important
16 element of test year regulation is the incentive for management to control and reduce
17 costs in order to earn its authorized return between rate cases.¹⁴

18 **Q. WHAT IS YOUR RESPONSE TO MR. BROSCH ON THAT ISSUE?**

19 A. While I agree with Mr. Brosch that management should be responsible for controlling
20 costs and operating efficiently, as discussed in the direct testimony of Company
21 witness Baxter, Ameren Missouri has taken many important steps in that regard.¹⁵ In

¹³ Ibid, at 9.

¹⁴ Ibid, at 5.

¹⁵ See direct testimony of Warner Baxter, at 14-15.

1 addition, Ameren Corporation has taken steps in recent years to conserve cash and to
2 align its capital spending with changes in economic conditions during the recent
3 recession. For example, Ameren Corporation reduced its dividend payment by
4 50 percent in 2009, issued new common equity to strengthen its balance sheet, and
5 reduced capital spending plans at Ameren Missouri in response to economic
6 conditions and lower customer demand for electric utility service. Notwithstanding
7 these efforts, Ameren Missouri has not had a reasonable opportunity to earn a fair
8 return since June 2007.

9 **Q. DO YOU AGREE WITH COMPANY WITNESS BARNES THAT FROM A**
10 **POLICY PERSPECTIVE REGULATORY LAG SHOULD APPLY**
11 **CONSISTENTLY AND IN A BALANCED WAY?**

12 A. Yes, I do. As Ms. Barnes discusses in her rebuttal testimony, other parties (including
13 Staff and MIEC) appear to suggest that when regulatory lag harms Ameren Missouri
14 it must be absorbed by the Company, but when regulatory lag benefits the Company,
15 then the benefit should be returned to ratepayers. This position is not consistent with
16 Mr. Brosch's view that regulatory lag provides an incentive for Ameren Missouri's
17 management to "control and reduce costs,"¹⁶ because when the regulatory lag benefits
18 the Company, other parties would have those benefits returned to ratepayers, which
19 removes the incentive to Ameren Missouri to reduce costs and operate more
20 efficiently. I agree with Ms. Barnes that, from a policy perspective, the ratemaking
21 process should treat the effects of regulatory lag consistently and in a balanced way. I

¹⁶ See direct testimony of Michael L. Brosch, at 5.

1 also agree that the Commission should take steps to mitigate the excessive regulatory
2 lag that Ameren Missouri has experienced.

3 **Q. DO YOU AGREE WITH MR. BROSCH THAT THE COMMISSION**
4 **AUTHORIZED ROE SHOULD BE VIEWED AS AN OPPORTUNITY TO**
5 **EARN, NOT A GUARANTEED LEVEL OF RETURN?**

6 A. Yes. As I explained in my direct testimony, equity investors need not be guaranteed a
7 specific return on their investment, but they should have a fair and reasonable
8 opportunity to realize a compensatory return.¹⁷ If a utility does not have a fair and
9 reasonable opportunity to earn its allowed ROE, particularly in a time of elevated
10 capital expenditures and weak sales, the utility will have more difficulty attracting
11 capital on reasonable terms to continue to fund investments required to provide safe
12 and reliable service at affordable rates. Ultimately, this is detrimental to customers.

13 ***EFFECTIVENESS OF MISSOURI REGULATION IN REDUCING REGULATORY LAG***

14 **Q. MR. BROSCH STATES THAT MISSOURI REGULATION PROVIDES A**
15 **NUMBER OF MEASURES THAT HAVE REDUCED OR ELIMINATED**
16 **REGULATORY LAG WHILE PROTECTING RATEPAYERS. WHAT IS**
17 **YOUR RESPONSE?**

18 A. I agree with Mr. Brosch that the Commission has approved certain cost recovery
19 mechanisms that reduce regulatory lag for Ameren Missouri; however, the evidence
20 demonstrates that the Company still has not had a reasonable opportunity to earn its
21 authorized ROE. This systemic and chronic problem suggests that the regulatory

¹⁷ See direct testimony of John J. Reed, at 15.

1 environment in Missouri has not kept up with fundamental changes that have
2 occurred in the electric utility industry. As discussed in my direct testimony,
3 technological improvements were previously driving unit costs down at the same time
4 that load growth was increasing revenues.¹⁸ As a result, costs to serve customers
5 were declining in some cases and revenue growth was able to keep pace with cost
6 growth where it occurred. Today, the exact opposite is true. The industry is in an
7 environment of rising costs and essentially flat or declining sales volumes per
8 customer.

9 Specifically, much of the equipment installed by Ameren Missouri during the
10 growth years from the 1970s to the 1990s now requires replacement or upgrading in
11 order to continue to provide safe and reliable service to customers. Further, the
12 Company is making capital investments in assets to comply with legislative
13 mandates, including environmental and renewable energy laws. All of these
14 investments are necessary and require additional capital, but none contribute to
15 revenue growth for Ameren Missouri. Absent modifications to the regulatory
16 framework in Missouri, the Company will continue to suffer from regulatory lag and
17 earnings attrition as a result.

18 **Q. DO YOU AGREE WITH MR. BROSCHE THAT REGULATION IN MISSOURI**
19 **IS CONSISTENT WITH METHODS USED IN MANY OTHER STATES?**¹⁹

20 A. No, however, the most important consideration is not whether Missouri's regulatory
21 environment is similar to or different than other jurisdictions, but whether the
22 Commission provides Ameren Missouri with a reasonable opportunity to recover its

¹⁸ Ibid, at 9.

¹⁹ See direct testimony of Michael L. Brosch, at 16.

1 prudently-incurred costs and earn its authorized ROE. While my direct testimony
2 provided numerous examples of methods that other states have used to reduce
3 regulatory lag, the purpose of my testimony is not simply to compare Missouri to
4 other jurisdictions, but rather to demonstrate that other regulatory authorities have
5 implemented cost recovery mechanisms that contribute to a reduction in regulatory
6 lag and earnings attrition.

7 *MISSOURI ECONOMIC CONDITIONS AND BUSINESS ENVIRONMENT*

8 **Q. DO YOU AGREE WITH MR. BROSCHE'S CHARACTERIZATION OF THE**
9 **BUSINESS ENVIRONMENT AS "GENERALLY FAVORABLE"?**

10 A. No, I do not. In support of his position, Mr. Brosch notes that current levels of
11 general inflation are relatively low, interest rates at which utilities can finance rate
12 base or re-finance outstanding debt are at historically low levels, and technological
13 improvements continue to drive productivity gains.²⁰ In my direct testimony, I
14 explained that the business environment for utilities depends primarily on two factors
15 – economic conditions and the regulatory environment.²¹ With respect to economic
16 conditions, I cited a report from the St. Louis Federal Reserve showing that Missouri
17 suffered more severely from the recent recession and has been slower to recover than
18 the remainder of the nation. Updated information from the same source continues to
19 demonstrate that economic conditions in Ameren Missouri's service territory are
20 relatively weak. The most recent report published by the St. Louis Federal Reserve
21 states:

²⁰ Ibid, at 15.

²¹ See direct testimony of John J. Reed, at 15.

1 The Philadelphia Fed's coincident index combines information on
2 payroll employment, wages, unemployment, and hours of work to give
3 a single measure of economic performance. The coincident indexes
4 for both Illinois and Missouri reveal a stronger impact of the recession
5 and a slower recovery in these states compared with the nation. In
6 fact, the index values during the recession show that, at the lowest
7 point, the level of economic activity in Illinois and Missouri was at
8 89.5 percent and 91.9 percent of pre-recession levels, respectively.
9 Meanwhile, the nation's lowest point of economic activity was at 95.3
10 percent of its pre-recession level. Current values of the index suggest
11 that, compared with pre-recession levels, economic activity in Illinois
12 is at 95.7 percent, while it is at 94.4 percent in Missouri and 101.2
13 percent in the nation.²²

14 Based on the above information, it is clear that economic activity in Missouri
15 remains below pre-recession levels, and that the recovery in Missouri is lagging the
16 rest of the nation. Furthermore, the Federal Reserve notes:

17 St. Louis's recession-related decline in employment, which was
18 centered near the first quarter of 2009, was similar to the nation's
19 decline. The recovery in St. Louis was also similar to the nation's
20 until the first quarter of 2011. After that point, employment growth in
21 St. Louis had been consistently below the nation's.²³

22 Therefore, it is not reasonable to expect that the business environment in Missouri
23 will somehow be so favorable that regulatory lag and earnings attrition are no longer
24 problems for Ameren Missouri.

²² Current Economic Conditions in the Eighth Federal Reserve District, St. Louis Zone, Research Division of the Federal Reserve Bank of St. Louis, June 22, 2012, at 5.

²³ Ibid, at 3.

1 **Q. WHAT IS YOUR RESPONSE TO MR. BROSCH'S CLAIM THAT FLAT OR**
2 **DECLINING SALES PER CUSTOMER DOES NOT MEAN THAT AMEREN**
3 **MISSOURI CANNOT EXPERIENCE GROWING SALES VOLUMES BY**
4 **ADDING NEW RESIDENTIAL AND COMMERCIAL CUSTOMERS AND**
5 **EXPANDING SALES TO LARGE INDUSTRIAL CUSTOMERS?**

6 **A.** Given the economic conditions discussed above, in conjunction with the industry
7 trend toward energy efficiency and conservation, it is not reasonable to assume that
8 Ameren Missouri will be able to earn its authorized return in the next few years
9 simply by adding new residential or commercial customers or by selling more
10 electricity to existing large industrial customers. What Mr. Brosch fails to recognize
11 is that Ameren Missouri's current capital investment focuses on replacing aging
12 infrastructure and complying with environmental requirements, both of which are
13 necessary, but neither of which produce additional revenues until the plant is added to
14 rate base in a future rate case. To the extent Ameren Missouri may have seen some
15 improvement in its earnings because of its continued cost-cutting measures, as Ms.
16 Barnes indicates in her rebuttal testimony, it is also not reasonable to expect the
17 Company to continue to cut both capital and operating and maintenance expenditures
18 and at the same time be able to address aging infrastructure issues in a way that would
19 benefit customers.

1 **PLANT-IN-SERVICE ACCOUNTING PROPOSAL**

2 **Q. PLEASE SUMMARIZE MR. GORMAN'S POSITION WITH RESPECT TO**
3 **AMEREN MISSOURI'S PLANT-IN-SERVICE ACCOUNTING PROPOSAL.**

4 A. Mr. Gorman states that the Plant-in-Service Accounting proposal fails to recognize
5 that the Company's rates may not need to be increased in order to provide for a fair
6 return on, and recovery of, the new investment costs.²⁴ According to Mr. Gorman,
7 simply because a utility places plant in service does not mean that its rates will
8 automatically need to be increased. As support for his position, Mr. Gorman cites the
9 period from 1987 through 2006 when Ameren Missouri did not increase its rates a
10 single time even though the Company's rate base grew from \$3.84 billion in 1987 to
11 \$5.6 billion in 2006. Mr. Gorman contends that Ameren Missouri's actual earnings
12 were not distressed during this time period despite the fact that there were no rate
13 increases.²⁵ On that basis, Mr. Gorman concludes that the fact that a utility is
14 increasing its plant in service does not necessarily indicate that the utility's rates will
15 not provide fair compensation to the utility for plant additions.

16 **Q. WHAT IS YOUR RESPONSE TO MR. GORMAN ON THIS ISSUE?**

17 A. The period from 1987 through 2006 for Ameren Missouri was characterized by
18 capital investments to serve new customer growth and increased demand for
19 electricity among existing customers. Mr. Gorman fails to consider that Ameren
20 Missouri's current capital investment spending principally involves replacement of
21 aging infrastructure and compliance with environmental requirements. The critical
22 distinction between the two periods is that the current capital investments do not

²⁴ See direct testimony and schedules of Michael P. Gorman, at 75.

²⁵ Ibid.

1 produce additional revenues for Ameren Missouri, whereas those from 1987-2006
2 did. During periods when electric utility revenues are increasing due to customer
3 growth and demand growth, the utility can often absorb the cost of rate base additions
4 without the need to raise customer rates for a period of time. Conversely, when
5 capital spending does not generate new revenues for the utility and demand growth is
6 stagnant, such as during the period since June 2007, the situation can contribute
7 toward significant earnings attrition because Ameren Missouri cannot start earning a
8 return on those investments until the plant is added to rate base in a future rate case.
9 In the interim, between the time when the plant is placed into service and the time
10 when the Company begins to recover those costs in rates, Ameren Missouri is
11 incurring depreciation expense on the new plant and is not earning a return on the
12 assets. Therefore, Mr. Gorman's point is mistaken because he fails to consider the
13 critical distinction between the current investment cycle and the growth-related period
14 from 1987-2006.

15 **Q. PLEASE SUMMARIZE MR. BROSCH'S POSITION WITH RESPECT TO**
16 **AMEREN MISSOURI'S PROPOSED PLANT-IN-SERVICE ACCOUNTING.**

17 A. Mr. Brosch states that Ameren Missouri has not shown that regulatory lag is a
18 significant ongoing problem that merits such "extraordinary and open-ended
19 piecemeal ratemaking."²⁶ Further, Mr. Brosch contends that Ameren Missouri's
20 Plant-in-Service Accounting proposal is poor regulatory policy because it would
21 remove the regulatory lag efficiency incentive that presently exists and that serves to
22 encourage management to carefully optimize budgets and control actual capital

²⁶ See direct testimony of Michael L. Brosch, at 18.

1 expenditures.²⁷ Moreover, Mr. Brosch claims that the proposed Plant-in-Service
2 Accounting mechanism would allow fairly automatic recovery of whatever amounts
3 are spent by Ameren Missouri on new qualifying capital additions.²⁸

4 **Q. WHAT IS YOUR RESPONSE TO MR. BROSCH ON THOSE ISSUES?**

5 A. First of all, Plant-in-Service Accounting is not ratemaking. To the contrary, it is
6 deferral accounting and any ratemaking will only take place in a future rate case when
7 the Company will, by adoption of the proposal, have the opportunity to include the
8 deferred amounts in rate base and recover them over the long lives of the assets.
9 With respect to Mr. Brosch's first point, Ameren Missouri has demonstrated that
10 regulatory lag has contributed to chronic earnings attrition since June 2007. In my
11 view, that earnings attrition is very likely to continue, absent a fundamental change in
12 the Missouri regulatory environment. As to Mr. Brosch's concern that the proposed
13 Plant-in-Service Accounting is poor regulatory policy because it removes the
14 incentive to control capital spending, Ameren Missouri's customers expect a certain
15 level of reliability and service quality. Under the present regulatory environment in
16 Missouri, the Company has very little incentive to undertake capital projects that
17 maintain system reliability beyond the basic requirements or to consider other
18 discretionary projects that might benefit customers (*e.g.*, smart metering). In
19 response to Mr. Brosch's third point, the substantial equivalent of Plant-in-Service
20 Accounting has already been approved by the Commission in Missouri for specific
21 projects. Cost recovery would continue to depend on whether the Commission
22 determined that the project was necessary and whether the costs were reasonable and

²⁷ Ibid, at 20.

²⁸ Ibid, at 20.

1 prudent. For these reasons, I believe that Mr. Brosch's concerns are overstated and
2 would serve to limit the ability of Ameren Missouri to earn its authorized ROE while
3 providing improved reliability and service quality to its customers.

4 **Q. ARE YOU AWARE OF ANY OTHER JURISDICTIONS THAT HAVE**
5 **APPROVED REGULATORY MECHANISMS THAT ARE SIMILAR OR**
6 **ANALOGOUS TO AMEREN MISSOURI'S PROPOSED PLANT-IN-**
7 **SERVICE ACCOUNTING?**

8 A. Yes, I am. The Indiana Utility Regulatory Commission ("URC") recently approved
9 the use of "post-in-service accounting" for Southern Indiana Gas and Electric
10 Company ("SIGECO"). As that accounting treatment was described in the testimony
11 of a company witness, Ms. M. Susan Hardwick, it would allow SIGECO to defer
12 depreciation expense on plant placed in service until the time when the assets are
13 included in rate base in the next rate case, and to continue to earn a return on the plant
14 at the AFUDC rate even after the plant is placed in service.²⁹ In approving this
15 accounting treatment, the Indiana URC stated: "We grant this request because of the
16 earnings erosion which would otherwise occur but also because of the significant
17 environmental and cost savings benefits that will immediately accrue to customers
18 from these projects."³⁰

²⁹ See prepared direct testimony and exhibits of M. Susan Hardwick, Cause No. 43839, filed December 11, 2009, at 34-35.

³⁰ Indiana Utility Regulatory Commission, Cause No. 43839, Final Order Approved April 27, 2011, at 103.

1 In addition, the Public Service Commission of South Carolina issued a
2 directive approving a request for an accounting order for post-in-service accounting
3 filed by Duke Energy Carolinas.³¹ According to the filing:

4 [Duke seeks] an accounting order for regulatory accounting purposes
5 authorizing the Company to defer in a regulatory asset account certain
6 post-in-service costs that are being or will be incurred in connection
7 with (1) the addition of the Allen Steam Station flue gas
8 desulfurization equipment ("FGD" or "scrubber") related to
9 environmental compliance (scheduled to go into service in the Spring,
10 2009), and (2) the purchase of a portion of Saluda River Electric
11 Cooperative, Inc.'s, ("Saluda River") ownership interest in the
12 Catawba Nuclear Station (completed in September, 2008). The costs
13 Duke Energy Carolinas is seeking to defer are the incremental costs
14 that are being or will be incurred from the date these assets are placed
15 in service and are used and useful in providing electric service to its
16 South Carolina retail customers to the date the Company is authorized
17 to begin reflecting in rates the recovery of such costs on an on-going
18 basis. The incremental costs for which this deferral treatment is
19 requested include depreciation, cost of capital, property taxes, and the
20 related non-fuel operation and maintenance expenses.³²

21 Furthermore, the State of Ohio has passed legislation that allows natural gas
22 utilities to request post-in-service accounting treatment. Finally, the Missouri
23 Commission has previously approved requests for "construction accounting" (which
24 is analogous to Plant-in-Service Accounting) for major projects, as described in the
25 direct testimony of Company witness Baxter.³³ As such, there is precedent in both
26 Missouri and other jurisdictions for the Company's proposed Plant-in-Service
27 Accounting. Importantly, the Indiana URC has determined that such accounting
28 treatment reduces earnings attrition, and provides benefits to customers.

³¹ See Docket No. 2009-55-E, issued February 25, 2009.

³² Duke Energy Carolinas, LLC, Petition for Accounting Order, Docket No. 2009-55-E, filed February 4, 2009.

³³ See direct testimony of Warner Baxter, at 25-26.

1 **Q. WHAT IS YOUR RESPONSE TO MR. BROSCH'S OBSERVATION THAT**
2 **AMEREN MISSOURI'S RATE BASE IS EXPECTED TO GROW VERY**
3 **LITTLE BETWEEN 2012 AND 2016, PARTICULARLY IN COMPARISON**
4 **WITH OTHER PORTIONS OF AMEREN CORPORATION?**³⁴

5 **A.** Mr. Brosch's observation is consistent with the assertion in my direct testimony that
6 because Ameren Missouri does not have a reasonable opportunity to earn its
7 authorized ROE, as evidenced by systemic and chronic under-earning since June
8 2007, the parent company (Ameren Corporation) has little incentive to invest in
9 Missouri beyond the basic requirements to maintain system reliability and service
10 quality.³⁵ Mr. Brosch appears to understand that situation, although he persists in his
11 belief that the regulatory environment in Missouri provides a number of measures that
12 have reduced or eliminated regulatory lag. Given Mr. Brosch's view regarding the
13 adequacy of the Missouri regulatory environment, it is unclear how he explains why
14 Ameren Missouri has not had a reasonable opportunity to earn its authorized ROE on
15 a weather-normalized basis. As noted earlier, the fact that the Company had adjusted
16 its expenditures in an effort to close the earnings gap is not necessarily good for
17 anyone, the Company or its customers, if the consequence is that beneficial
18 replacement of aging infrastructure or other service needs are under-funded. Mr.
19 Brosch's clients may get a short-term "benefit" from slightly lower rates, but his
20 clients and customers generally are likely to suffer intermediate and longer-term
21 detriments. I would also note that, given how sums accrued and deferred under the
22 Company's Plant-in-Service Accounting proposal would ultimately be accounted for

³⁴ See direct testimony of Michael L. Brosch, at 24.

³⁵ See direct testimony of John J. Reed, at 31.

1 in rates (in a later rate case where the Commission considers that issue), the impact on
2 customer rates would be fairly minor, given that the sums would be capitalized with
3 the recovery to occur over the long lives of the assets which were placed in-service.

4 ***CREDIT RATING AGENCIES' ASSESSMENT OF REGULATORY RISK***

5 **Q. DO YOU AGREE WITH MR. GORMAN THAT CREDIT RATING**
6 **AGENCIES HAVE A FAVORABLE VIEW OF THE REGULATORY**
7 **ENVIRONMENT IN MISSOURI?**

8 A. No, I do not. As Mr. Gorman correctly observes, the Missouri regulatory
9 environment is rated as below average by the leading credit rating agencies.³⁶ While
10 Mr. Gorman is correct that Standard and Poor's ("S&P") has indicated that the
11 regulatory environment in Missouri has been improving in recent years, S&P
12 continues to rank the Missouri regulatory environment as "less credit supportive."³⁷
13 Likewise, as discussed in my direct testimony, Moody's Investors Service
14 ("Moody's") continues to raise concerns about regulatory lag for Ameren Missouri,
15 even after the Commission's decision in the last electric rate case (Case No. ER-
16 2011-0028), stating:

17 Union Electric operates in what Moody's has considered to be a below
18 average regulatory framework, which has resulted in significant
19 regulatory lag and prevented the utility from earning its allowed return
20 on equity. Factors contributing to Moody's below average regulatory
21 assessment include lengthy 11 month base rate case timelines; the lack
22 of interim rate relief; the use of historical test years; and less than full
23 recovery of fuel costs.³⁸

³⁶ See direct testimony of Michael P. Gorman, at 61.

³⁷ Standard and Poor's, Updates Its U.S. Utility Regulatory Assessments, March 12, 2010, at 1.

³⁸ Moody's Investor Service, Credit Opinion: Union Electric Company, August 12, 2011, at 2.

1 **Q. PLEASE SUMMARIZE MR. GORMAN’S POSITION WITH REGARD TO**
2 **HOW WELL CREDIT RATING AGENCIES HAVE DEFINED THE**
3 **EVALUATION OF REGULATORY RISK AND THE ASSESSMENT OF**
4 **REGULATORY ENVIRONMENTS.**

5 A. Mr. Gorman contends that credit rating agencies have not defined the term
6 “regulatory risk,” and he argues that it is critical to understand how the credit rating
7 analysts assign a regulatory environment rating before giving the rating significant
8 weight in deciding whether a change to Missouri’s regulatory framework is
9 justified.³⁹ Further, Mr. Gorman states that from a regulatory perspective, credit
10 analysts are primarily focused on whether or not costs are recovered in rates, and not
11 whether the cost was prudent or imprudent and appropriate to be included in rates.⁴⁰
12 For that reason, Mr. Gorman contends that more details need to be offered to explain
13 how rating agencies establish the regulatory ranking before the Commission places
14 weight on the credit rating agencies’ assessment of regulatory risk.

15 **Q. DO YOU AGREE WITH MR. GORMAN THAT CREDIT RATING**
16 **AGENCIES HAVE NOT DEFINED THE TERM “REGULATORY RISK”**
17 **AND HAVE NOT EXPLAINED HOW THEY ASSESS THE REGULATORY**
18 **ENVIROMENT?**

19 A. Absolutely not. In my direct testimony, I cited publications from Moody’s and S&P
20 that explain how those credit rating agencies assess regulatory risk. While neither
21 rating agency attempts to quantify regulatory risk, they both provide numerous factors
22 which they consider as part of their assessment and evaluation of regulatory risk for

³⁹ See direct testimony and schedules of Michael P. Gorman, at 62.
⁴⁰ Ibid.

1 regulated electric and natural gas utilities. For example, in developing its credit
2 rating, Moody's assigns 50 percent weight to the regulatory environment in which the
3 utility operates. Specifically, Moody's evaluates the regulatory framework and the
4 cost recovery mechanisms in its assessment of regulatory risk. In terms of the
5 regulatory framework, Moody's considers the following factors: (1) regulatory
6 independence; (2) level of development of the regulatory framework; (3)
7 predictability; (4) alternative rate making mechanisms; and (5) a utility's business
8 model.⁴¹ With regard to cost recovery provisions, Moody's looks at the following
9 factors: (1) return on equity and regulatory lag; (2) fuel, purchased power, and other
10 automatic adjustment clauses; (3) forecast risk – historical vs. forward test years;
11 (4) regulatory pre-approvals; (5) construction work in progress in rate base;
12 (6) interim rate relief; (7) volume risk and decoupling; and (8) cost recovery bonds
13 (securitization).⁴²

14 **Q. PLEASE DISCUSS THE FACTORS THAT S&P CONSIDERS IN ASSESSING**
15 **AND RANKING REGULATORY ENVIRONMENTS.**

16 A. S&P ranks regulatory environments based on factors similar to those used by
17 Moody's to evaluate regulatory risk. Specifically, S&P states: "the foundation of our
18 opinion of the regulation in a jurisdiction is the degree to which competitive market
19 forces are allowed to influence rates."⁴³ After identifying the fundamental regulatory
20 paradigm, S&P's analysis considers factors that influence the utility's business risk

⁴¹ Regulatory Frameworks – Ratings and Credit Quality for Investor-Owned Utilities; Moody's Investors Service, June 18, 2010.

⁴² Cost Recovery Provisions Key to Investor Owned Utility Ratings and Credit Quality, Moody's Investors Service, June 18, 2010.

⁴³ Assessing U.S. Utility Regulatory Environments, Standard and Poor's Global Credit Portal, March 11, 2010, at 3.

1 climate in the jurisdictions, including: (1) ratemaking practices and procedures; (2)
2 political insulation; and (3) cash flow support and stability.⁴⁴

3 In terms of ratemaking practices and procedures, S&P's assessment focuses
4 on the jurisdiction's overall approach to setting rates and the process it uses to
5 conduct and manage base rate filings. S&P states: "In this part of the assessment, we
6 concentrate on whether established base rates fairly reflect the cost structure of a
7 utility and allow management an opportunity to earn a compensatory return..."⁴⁵
8 S&P continues: "Notably, the analysis does not revolve around 'authorized' returns,
9 but rather on actual earned returns. We note the many examples of utilities with
10 healthy authorized returns that, we believe, have no meaningful expectation of
11 actually earning that return because of rate case lag, expense disallowances, etc."⁴⁶
12 Other ratemaking factors that S&P considers include the authorized capital structure,
13 the timeliness of rate decisions, an evaluation of the test year, the timing of interim
14 rates, regulatory oversight of large capital projects, and the use of non-traditional
15 ratemaking practices such as weather normalization and incentive ratemaking. In
16 discussing regulatory lag, S&P notes: "We do not view the issue of regulatory lag as
17 an intermittent concern, consequential only during times of acute inflation or rising
18 capital spending, but as a consistent part of our credit analysis."⁴⁷

19 According to S&P, political insulation measures the extent to which the
20 setting of utility rates is influenced by political as well as economic factors. Among
21 the factors that S&P considers in this part of the assessment are the method of

⁴⁴ Ibid.

⁴⁵ Ibid., at 4.

⁴⁶ Ibid., at 4.

⁴⁷ Ibid., at 4.

1 selecting utility commissioners, the involvement of the executive or legislative branch
2 in utility matters, the history and tradition of independence accorded to the regulatory
3 body, and the behavior of important constituent groups that intervene in utility
4 proceedings.

5 Finally, S&P considers the cash flow support and stability of the regulatory
6 environment. The most prominent factor in this part of the analysis is the application
7 of separate tariff provisions for major expenses such as fuel and purchased power.
8 S&P also analyzes the quality of special tariff mechanisms to determine their
9 effectiveness in producing cash flow stability. In addition, S&P considers a
10 commission's rate design decisions, such as the relative size of the monthly customer
11 charge, and the prevalence of decoupling mechanisms. Further, S&P notes that
12 especially during upswings in the capital expenditure cycle, a jurisdiction's
13 willingness to support large capital projects during the construction phase is an
14 important aspect of its analysis. In today's environment of rising construction costs
15 and possible inflationary pressures, S&P indicates that cash flow support could be
16 crucial in maintaining credit quality through the spending program.⁴⁸

17 ***OTHER ISSUES***

18 **Q. WHAT IS YOUR RESPONSE TO MR. GORMAN'S POSITION THAT THE**
19 **FACT THAT OTHER JURISDICTIONS MAY HAVE A SHORTER RATE**
20 **CASE TIMELINE DOES NOT NECESSARILY MEAN THAT UTILITIES IN**
21 **OTHER JURISDICTIONS DEVELOP RATES MORE EFFICIENTLY, NOR**

⁴⁸ Ibid, at 6.

1 **DOES IT MEAN THAT OTHER UTILITIES HAVE A BETTER**
2 **OPPORTUNITY TO EARN THEIR AUTHORIZED RETURNS?**

3 A. To the extent that utilities in other jurisdictions are able to implement new rates in
4 less time than the eleven months that it typically takes for Ameren Missouri, those
5 utilities have a better opportunity to earn their authorized returns because cost
6 recovery is more timely. For example, if O&M costs have increased by three percent
7 since the last rate case, it would be more advantageous from the utility's perspective
8 if the rate case were completed in six months rather than eleven months because the
9 utility would have the opportunity to begin recovering those higher O&M costs
10 through customer rates. Rate case lag contributes to earnings attrition insofar as the
11 utility's actual cost of service is higher than the amount embedded in current rates.
12 For that reason, I disagree with Mr. Gorman's position on this issue.

13 **Q. PLEASE SUMMARIZE MR. GORMAN'S TESTIMONY WITH RESPECT TO**
14 **THE RELATIVE ADVANTAGES OF HISTORICAL AND FORECASTED**
15 **TEST YEARS.**

16 A. Mr. Gorman contends that the Missouri regulatory procedures that prescribe an
17 historical test year are not necessarily a disadvantage to either investors or
18 ratepayers.⁴⁹ In support of his position, Mr. Gorman states that Missouri allows for a
19 true-up of historical costs based on known and measurable changes, so that the data
20 used to develop rates in Missouri are typically no more than six months stale by the
21 time rates go into effect.⁵⁰ Further, Mr. Gorman states that future test years are
22 notoriously unreliable and may over- or understate actual costs, revenues, sales and

⁴⁹ See direct testimony and schedules of Michael P. Gorman, at 69-70.
⁵⁰ Ibid.

1 capital investments during the test year and the period rates will be in effect.⁵¹

2 Moreover, Mr. Gorman testifies that Missouri uses an end-of-period rate base, which
3 he claims is more advantageous to the utility than the average rate base typically used
4 in a forecasted test year.⁵²

5 **Q. WHAT IS YOUR RESPONSE TO MR. GORMAN ON THIS ISSUE?**

6 A. As explained in my direct testimony, many jurisdictions use a forecasted test year to
7 set rates in order to more accurately reflect projected revenues, costs and investments
8 during the period in which rates will be in effect.⁵³ To the extent that forecasted
9 amounts are different than historical amounts, a historical test year will fail to be
10 representative of those differences. While I agree with Mr. Gorman that Missouri
11 adjusts historical costs based on known and measurable changes that occur after the
12 end of the test year, the fact remains that those costs are outdated by the time new
13 rates become effective.⁵⁴ As to Mr. Gorman's concern that forecasted test years are
14 unreliable, many jurisdictions have addressed the potential for forecasting error by
15 requiring the utility to file both actual, historical costs and forecasted costs. To the
16 extent that actual costs are different than forecasted costs, the regulatory authority can
17 use variance accounts to adjust future rates. In response to Mr. Gorman's final point,
18 I strongly disagree that the use of an end-of-period rate base for a historical test year
19 is more advantageous for a utility than the average rate base typically used for a
20 forecasted test year. If the utility is making significant capital investments, the end-

⁵¹ Ibid.

⁵² Ibid.

⁵³ See direct testimony of John J. Reed, 38.

⁵⁴ With respect to O&M expenditures, when the cost trend is up, simply using an historical 12-month period through a true-up date that will be five to six months old by the time rates take effect will almost certainly mean that the cost levels assumed when rates were set will be too low almost immediately when rates take effect, or perhaps even before rates take effect.

1 of-period rate base for an historical test year will not reflect any additional dollars that
2 were invested in utility plant during the forecasted test year. Under that scenario, the
3 utility would not have an opportunity to earn a return on assets that have been placed
4 in service after the end of the historical test period, even if those assets are placed in
5 service before new rates become effective.

6 **Q. DO YOU AGREE WITH MR. GORMAN'S CLAIM THAT THE USE OF AN**
7 **HISTORICAL TEST YEAR HAS GENERALLY SUPPORTED AMEREN**
8 **MISSOURI'S ABILITY TO SET RATES THAT MEET THE COMPANY'S**
9 **EARNINGS OBJECTIVES OVER LONG PERIODS?**

10 A. No, I do not. While Ameren Missouri was, in fact, making large capital investments
11 from 1987-2006, those investments were attributable to customer growth and load
12 growth. As a result, Ameren Missouri was able to earn higher revenues, even if there
13 was some regulatory lag between the time when those assets were placed in service
14 and the time the Company was allowed to include them in rate base because new
15 customers were being added to the system and existing customers were using more
16 electricity. However, as discussed throughout my direct and rebuttal testimony, the
17 opposite is now true. From my perspective, the deficiencies of an historical test year
18 were masked during that earlier period, but due to fundamental changes in the energy
19 industry, those deficiencies are now apparent in the form of earned returns that lag
20 well behind the Company's authorized ROE.

1 **IV. CONCLUSIONS AND RECOMMENDATIONS**

2 **Q. PLEASE SUMMARIZE YOUR CONCLUSIONS AND**
3 **RECOMMENDATIONS.**

4 **A.** My conclusions and recommendations are:

- 5 • Ameren Missouri has been denied a reasonable opportunity to earn its allowed
6 return for years. Even after taking into consideration regulatory adjustments, the
7 Company has generally been unable to earn its allowed return on a weather-
8 normalized basis since June 2007.
- 9 • Ameren Missouri's rates are out-of-date the moment they become effective and,
10 as a result, the Company is forever denied the opportunity to recover costs it
11 incurs to serve its customers. Absent modifications to the regulatory framework
12 in Missouri, the Company will continue to suffer from regulatory lag and earnings
13 attrition.
- 14 • Other jurisdictions have approved regulatory mechanisms that are analogous to
15 Ameren Missouri's Plant-in-Service Accounting proposal, and have noted that
16 such mechanisms reduce earnings attrition and benefit customers. In addition, the
17 Commission has previously approved "construction accounting" treatment for
18 major construction projects in Missouri.
- 19 • The Commission's adoption of the Plant-in-Service Accounting treatment and the
20 proposed two-way storm restoration cost tracker will provide Ameren Missouri
21 with a more reasonable opportunity to earn its authorized ROE and ultimately will
22 benefit the Company's customers through a more reliable electric system at rates
23 that remain among the lowest in the nation.

1 • I continue to recommend strongly that the Commission approve the Company's
2 proposed Plant-in-Service Accounting treatment and storm cost tracker and
3 continue the Company's existing rider and tracking mechanisms, as well as the
4 revised 10.50% ROE recommendation of Company witness Hevert.

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

6 **A. Yes, it does.**

In the Matter of Union Electric Company d/b/a)
Ameren Missouri's Tariffs to Increase Its Revenues) **Case No. ER-2012-0166**
for Electric Service.)

COMMONWEALTH OF MASSACHUSETTS)
) ss
COUNTY OF MIDDLESEX)

1. My name is John J. Reed and my office is located in Marlborough, Massachusetts and I am Chairman and Chief Executive Officer of Concentric Energy Advisors, Inc. and CE Capital Advisors, Inc. (together "Concentric").

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

Subscribed and sworn to before me this 14th day of August, 2012.

My commission expires: 10/15/15



JOANNE P. BICKFORD
NOTARY PUBLIC
COMMONWEALTH OF MASSACHUSETTS
MY COMMISSION EXPIRES
OCTOBER 15, 2015

