STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Ameren Illinois Company	:	
d/b/a Ameren Illinois	:	
	:	**12-0001**
Rate MAP-P Modernization Action	:	
Plan - Pricing Filing.	:	

ORDER

September 19, 2012

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By the Commission:

I. INTRODUCTION

On January 3, 2012, Ameren Illinois Company d/b/a Ameren Illinois ("AIC") filed with the Illinois Commerce Commission (“Commission”) a verified petition under Section 16-108.5 of the Public Utilities Act ("Act"), 220 ILCS 5/1-101 et seq., requesting approval of its Modernization Action Plan-Pricing tariff ("Rate MAP-P") as well as changes to other tariffs affected by such. Rate MAP-P represents AIC's efforts to implement recent revisions to the Act permitting it and Commonwealth Edison Company ("ComEd") to upgrade and modernize their respective electric transmission and distribution ("T&D") infrastructure through development of a "smart grid." Pursuant to Section 16-108.5(b)(2) of the Act, AIC is to invest $625,000,000 over a ten-year period in electric system upgrades, modernization projects, training facilities, and other smart grid upgrades. New provisions in the Act establish standards for recovery of the investments from ratepayers.

AIC posted a notice of the filing of the proposed rate changes in its Peoria business office and published a notice twice in newspapers of general circulation within each of its service areas, in accordance with the requirements of Section 9-201(a) of the Act, and the provisions of 83 Ill. Adm. Code 255, “Notice Requirements for Change in Rates for Cooling, Electric, Gas, Heating, Telecommunications, Sewer or Water Services.”

On January 31, 2012, the Administrative Law Judges sent AIC a list of deficiencies in its filing in accordance with 83 Ill. Adm. Code 285, "Standard Information Requirements for Public Utilities and Telecommunications Carriers in Filing for an Increase in Rates" ("Part 285"). AIC responded to the deficiency letter on February 24, 2012.

Petitions seeking leave to intervene were filed by the Citizens Utility Board (“CUB”) and AARP. Best Buy Co., Inc., J.C. Penney Corporation, Inc., Macy’s, Inc., Sam’s West, Inc., and Wal-Mart Stores, Inc. petitioned to intervene as the Commercial Group. Air Products and Chemicals Company, Archer-Daniels-Midland Company, Caterpillar, Inc., CCPS Transportation LLC, GBC Metals, LLC, Keystone Consolidated Industries, Inc., Marathon Petroleum Company, LP, Olin Corporation, Tate and Lyle Ingredients Americas, Inc., University of Illinois, Viscofan USA, Inc. and Washington Mills Hennepin, Inc. also intervened as members of the Illinois Industrial Energy Consumers ("IIEC"). All of the petitions to intervene were granted. The Office of the Attorney General entered an appearance on behalf of the People of the State of Illinois. Commission Staff ("Staff") participated as well.

Pursuant to due notice, status hearings were held in this matter before duly authorized Administrative Law Judges of the Commission at its offices in Springfield, Illinois on January 17 and June 18, 2012. Thereafter, evidentiary hearings were held June 20, 21, 22, and 25, 2012. Appearances were entered by counsel on behalf of AIC, Staff, the AG, CUB, AARP, IIEC, and the Commercial Group.

At the evidentiary hearings, AIC called 12 witnesses to testify. The 12 witnesses include (1) Michael Getz, AIC's Controller, (2) David Heintz, a Vice President of the consulting firm Concentric Energy Advisors, Inc., (3) Leonard Jones, AIC's Manager of Rates and Analysis, (4) Ryan Martin, Assistant Treasurer and Manager of Corporate Finance for Ameren Services Company ("AMS")[1] and Assistant Treasurer for AIC, (5) Robert Mill, AIC's Director of Regulatory Policy and Rates, (6) Craig Nelson, AIC's Senior Vice President of Regulatory Affairs and Financial Services, (7) Stan Ogden, AIC's Vice President of Customer Service and Metering Operations, (8) Ronald Pate, AIC's Vice President of Operations and Technical Services, (9) Ryan Schonhoff, a Regulatory Consultant within AIC, (10) Ronald Stafford, AIC's Manager of Regulatory Accounting, (11) Scott Verbest, Executive Compensation Lead for AMS,[2] and (12) James Warren, a tax attorney with the law firm of Miller & Chevalier Chartered.

Ten witnesses testified on behalf of Staff. The Staff witnesses include (1) Mary Everson, (2) Dianna Hathhorn, (3) Burma Jones, (4) Daniel Kahle, (5) Bonita Pearce, and (6) Scott Tolsdorf, Accountants in the Accounting Department of the Financial Analysis Division of the Commission's Bureau of Public Utilities, (7) Michael McNally and (8) Rochelle Phipps, Senior Financial Analysts in the Finance Department of the Financial Analysis Division, (9) William Johnson, an Economic Analyst in the Rate Department of the Financial Analysis Division, and (10) Samuel McClerren, an Engineering Analyst in the Rates Department.

IIEC offered three witnesses at the evidentiary hearings. IIEC's witnesses include Michael Gorman, Stephen Rackers, and Robert Stephens from the consulting firm Brubaker & Associates, Inc. Michael Brosch, a principal with Utilitech, Inc., a consulting firm engaged primarily in utility rate and regulation work, and David Effron, a consultant specializing in utility regulation, testified on behalf of the AG and AARP. Ralph Smith, a certified public accountant and senior regulatory utility consultant with

[1] AMS is the service company subsidiary of Ameren and provides various services to its affiliates, including AIC.
[2] Mr. Verbest adopted the prepared direct testimony of Krista Bauer, Manager of Talent Management and Executive Compensation for AMS.

the consulting firm Larkin & Associates, PLLC, and Christopher Thomas, a regulatory economics consultant, testified for CUB.

AIC, Staff, CUB, IIEC, and the Commercial Group each filed an Initial Brief and Reply Brief. The AG and AARP jointly filed an Initial Brief and Reply Brief. A Proposed Order was served on the parties. AIC, Staff, CUB, and IIEC each filed a Brief on Exceptions. The AG and AARP jointly filed a Brief on Exceptions. The statutory deadline in this matter did not permit time for Briefs in Reply to Exceptions. The Briefs on Exceptions were considered in the preparation of this Order. On September 11, 2012, AIC filed a petition for interlocutory review concerning an evidentiary motion granted by the ALJs striking portions of Ameren's Brief on Exceptions making reference to House Resolution 1157, adopted by the Illinois General Assembly's House of Representatives on August 17, 2012. The Commission granted Ameren's petition for interlocutory review at its September 19, 2012 bench session and allowed House Resolution 1157 to be included as evidence of legislative intent. This Order, and the analyses and conclusions reached herein, gives the resolution the weight afforded to it under the governing jurisprudence.

II. NATURE OF AIC'S OPERATIONS

Ameren Corporation ("Ameren") formed in 1997 with the merger of Union Electric Company and Central Illinois Public Service Company ("CIPS"). Thereafter, Ameren acquired Central Illinois Light Company ("CILCO") in 2002 and Illinois Power Company ("IP") in 2004. The service area of AIC covers roughly the lower two-thirds of Illinois. AIC currently serves approximately 1.2 million electric customers and 840,000 natural gas customers. All of AIC's operations are within Illinois, although an affiliate of AIC (Ameren Missouri Company ("AMC") f/k/a Union Electric Company d/b/a AmerenUE) provides utility service in Missouri. At one time, AMC's predecessor company served the St. Louis Metro East area in Illinois. That area was later subsumed within the service area of AmerenCIPS. Other affiliates of AIC provide unregulated services. Effective October 1, 2010, AmerenCILCO and AmerenIP merged with and into AmerenCIPS, resulting in AmerenCIPS being the sole surviving legal entity. Simultaneously, AmerenCIPS' name was changed to Ameren Illinois Company d/b/a Ameren Illinois. AIC identifies the former service areas of AmerenCIPS, AmerenCILCO, and AmerenIP as Rate Zone 1, Rate Zone 2, and Rate Zone 3, respectively.

III. OVERVIEW OF 16-108.5 RATE PROCESS

The recent revisions to the Act made by Public Acts 97-0616 and 97-0646 provide that an electric utility that commits to undertake an infrastructure investment program pursuant to Section 16-108.5(b) may elect to recover its delivery services costs through a performance-based rate approved by the Commission. The performance-based rate tariff (for AIC, Rate MAP-P) sets forth a formula for calculating a delivery service revenue requirement that will be used to set delivery service charges for retail electric customers. The formula includes the specific cost components that form the basis of the rates charged to the utility's delivery service customer classes. The performance-based rate provides for recovery of a utility's actual, prudently incurred and reasonable costs of electric delivery services, except for those costs that the utility continues to recover through automatic adjustment clause tariffs. The performance-based rate also reflects the utility's actual capital structure for the applicable year (excluding goodwill) and includes a cost of equity, the calculation of which is addressed in Section 16-108.5. The performance-based rate is intended to operate in a standardized and transparent manner and be updated annually to reflect (i) historical data from the most recently filed Federal Energy Regulatory Commission ("FERC") Form 1, plus projected plant additions and correspondingly updated depreciation reserve and depreciation expense for the year of filing, (ii) a reconciliation of the revenue requirement reflected in rates for each year, with what the revenue requirement would have been had the actual cost information for the year been available at the filing date, and (iii) any adjustments, including adjustments to reflect an earned rate of return on common equity outside the statutory range, required by Section 16-108.5(c). The rates established under this framework are "performance-based" because the ability to use this rate mechanism is dependent on the utility achieving certain metrics and performance goals for the periods they are in effect. AIC's most recently filed FERC Form 1 data from 2010 is the starting point for Rate MAP-P. The initial rates under Rate MAP-P will go into effect during the fourth quarter of 2012. As a distributor of electricity and natural gas, AIC is a "combination utility" under the revisions to the Act.

IV. AIC'S PROPOSED REVENUE REQUIREMENTS

AIC's proposed initial formula rate delivery service revenue requirement results in an overall decrease of $19.3 million from the electric revenue requirement last ordered by the Commission in Docket Nos. 09-0306 et al. (Cons.). The revenue requirement change by Rate Zone results in overall decreases of $10.1 million and $20.1 million for Rate Zones 1 and 3, respectively, and an increase of $10.9 million for Rate Zone 2. AIC's calculations use a rate of return of 9.019%.

AIC's most recent electric delivery service rate cases considered by the Commission were consolidated Docket Nos. 09-0306 through 09-0308. The Commission entered the Order in that matter on April 29, 2010. Shortly thereafter the Commission corrected calculation errors and entered on May 6, 2010 a Corrected Order authorizing a total aggregate electric revenue increase for AIC of approximately $35,175,000; substantially less than the approximately $115,000,000 electric rate increase that AIC sought at the close of the December 2009 evidentiary hearing in that proceeding. On November 4, 2010, the Commission entered an Order on Rehearing authorizing an additional $21,616,000, for a final total aggregate electric revenue increase of $56,791,000.

V. RATE BASE

A. Overview

The fundamental premise of the formula rate process is to set rates to recover AIC's actual costs of service during specific rate periods, through a combination of (a) rates based on projected costs for that period and (b) later reconciliation charges or credits intended to achieve a match with the utility's reported actual costs during that same period. (See Section 16-108.5(d)(1)). AIC's capital costs are a major component of that revenue requirement, and they must be measured accurately if the Commission is to set just and reasonable rates that reflect only AIC's prudently incurred, reasonable costs.

B. Uncontested Issues

1. Gross Plant in Service (except for C.8)

AIC has included $5,185,572,000 total plant in service after projected plant additions in rate base, which no party has taken exception to in this proceeding. The Commission finds this proposed adjustment to be reasonable, and it will be adopted for the purposes of this proceeding.

2. Accumulated Depreciation

AIC proposed an adjustment to accumulated depreciation, after projected plant additions, which reduces rate base by $2,464,105,000. No party to this proceeding took exception to this adjustment. The Commission finds this proposed adjustment to be reasonable, and it will be adopted for the purposes of this proceeding.

3. Plant Held for Future Use

In its direct testimony, Staff proposed a $3,000 deduction to rate base for Allowance for Funds Used During Construction ("AFUDC") amounts incorrectly charged to AIC's Property Held for Future Use balance. AIC acknowledged that the correction was not made until after 2010, therefore it was not reflected on its Property Held for Future Use Rate Base Information Appendix. AIC adopted Staff's proposal for this proceeding. The Commission finds this proposed adjustment to be reasonable, and it will be adopted for the purposes of this proceeding.

4. ADIT – Deferred Compensation

This balance of Accumulated Deferred Income Taxes ("ADIT") represents deferred taxes on accruals for deferred compensation in excess of amounts currently deductible for income taxes. AIC explains that the accrued liability for deferred compensation at AIC is related to CILCO Deferred Compensation for participants who retired prior to its acquisition by Ameren. In response to AG DR 2.10, AIC stated that

“AIC no longer considers the deferred compensation ADIT to be applicable to the current cost of providing service to electric distribution customers, and intends to remove the ADIT balance from jurisdictional rate base in its Rebuttal Filing.” AG/AARP witness Effron proposed an adjustment to remove the ADIT on this deferred compensation from rate base. Removal of this deferred tax debit balance reduces AIC's delivery services rate base by $2,924,000. The adjustment was adopted by AIC in its Ex. 13.1, App 4, column (C), lines 1 and 2. The Commission finds this proposed adjustment to be reasonable, and it will be adopted for the purposes of this proceeding.

5. Materials and Supplies

Staff recommends that AIC modify its calculation of materials and supplies included in rate base from a year-end balance to a 13-month average. Staff witness Jones stated since the balance of the materials and supplies account fluctuates from month to month, a 13-month average balance (December through December) evens out the highs and lows that occur throughout the year and provides a more reasonable amount to include in the rate base on which AIC earns a return. AIC indicated that it accepted this adjustment. The Commission finds this proposed adjustment to be reasonable, and it will be adopted for the purposes of this proceeding.

6. Cash Working Capital – Employee Benefits/Payroll Lead

AIC in its computation of cash working capital ("CWC") included calculations of payment dates and amounts for each element of employee benefits, including Medical and Dental plan payments, life insurance funding, 401k funding, and pension plan funding. In compiling the overall Employee Benefits lag day value, it appears that AIC did not include the calculated payment lag data for pensions. To more completely account for cash flow patterns associated with Employee Benefits, AG/AARP witness Brosch included AIC's calculations capturing the timing of pension funding payments within the test year Employee Benefits lag day value. On rebuttal, AIC agreed to the proposed adjustment to change the expense lead associated with pension expense, which increased the expense lead from 12.69 days to 15.97 days. The Commission finds this proposed adjustment to be reasonable, and it will be adopted for the purposes of this proceeding.

7. Customer Advances

AIC deducted $24,222,000 from rate base for Customer Advances, which represents the balance of cash advances received from customers as of December 31, 2010 for construction attributable to AIC’s electric delivery services operations. AIC indicates that no party contested this amount. The Commission finds this proposed adjustment to be reasonable, and it will be adopted for the purposes of this proceeding.

8. Customer Deposits

AIC's reduced its proposed rate base by $28,829,000 for customer deposits, and indicates it calculated this amount by utilizing the 13-month average of the total amount of jurisdictional customer deposits. AIC suggests that the use of a 13-month average balance corresponds with inclusion of 2010 interest on customer deposits in operating expense in the formula rate template consistent with the Commission's Orders in prior AIC rate cases. AIC also included an adjustment to add $144,000 to customer accounts expense for interest on customer deposits. AIC indicates that no party to this proceeding contested this issue. The Commission finds this proposed adjustment to be reasonable, and it will be adopted for the purposes of this proceeding.

9. OPEB Liability

AIC states that it proposed an adjustment to reduce rate base by $71,858,000 for other post-employment benefits ("OPEB") liability, and indicates that no party to this proceeding contested this adjustment. The Commission finds this proposed adjustment to be reasonable, and it will be adopted for the purposes of this proceeding.

C. Contested Issues

1. Cash Working Capital

a. Pass-Through Taxes Revenue Lag

i. AIC Position

AIC proposes a revenue lag of 34.54 days for pass-through taxes, specifically, Energy Assistance Charges ("EAC") and the Municipal Utility Tax ("MUT"), in its CWC calculation. As AIC witness Heintz explains, this reflects the actual treatment of pass-through tax collections and remittances by AIC. Staff, AG/AARP, and IIEC all recommend that the revenue lag period associated with pass-through taxes included in AIC's CWC determination be set to zero days.

AIC suggests that the crux of the dispute with respect to the EAC is whether AIC's CWC calculation should reflect the amount of time that AIC could hold pass-through taxes under the statutory remittance requirement, or the amount of time that AIC actually does hold the pass-through taxes before remitting. AIC indicates that its CWC amounts reflect the latter, which it claims is consistent with the Commission's Order in Docket No. 11-0282, which expressly rejected Staff's proposal to use zero lag days for EAC in AIC's last gas rate case. In its Order, AIC states the Commission concluded, "Given the circumstances surrounding the EAC, the Commission does not believe that the adjustment sought by Staff is warranted. The Commission will revisit this issue, however, if AIC alters its EAC remittance schedule." AIC asserts that as it has not altered its EAC remittance schedule since that time, there is no need to adjust AIC's treatment of pass-through taxes.

AIC notes that Staff witness Kahle and IIEC witness Rackers base their argument on the assertion that AIC is remitting the taxes before it is statutorily required to do so; however, AIC complains that this is merely a conceptual argument that AIC could hold the EAC funds for 35 days. As Mr. Heintz explains, the CWC requirement attributable to pass-through taxes should be based solely upon the actual time during which AIC has access to funds and the date the funds are remitted to the taxing authority. AIC notes it has one revenue source by which it collects the funds associated with the pass-through taxes and that is customers' payment of their monthly utility bills, and customers do not remit the portion of the bill associated with pass-through taxes at an earlier time than their regular bill.

AIC argues that Mr. Kahle's proposed treatment of pass-through taxes, for CWC purposes, fails to accurately reflect the time that AIC actually has access to the funds. The evidence AIC has presented in this proceeding measures this time, and reflects AIC's actual practice. AIC notes that Mr. Kahle acknowledged at hearing that, under AIC's actual remittance practice, AIC only has access to the EAC funds for 4 days and the MUT funds for only 14 days. AIC argues the CWC calculation should reflect this, and the Commission should continue to utilize AIC's actual remittance practice, as it did in Docket No. 11-0282. To the extent the witnesses opposing AIC's position of pass-through taxes all cite to Docket Nos. 09-0306 et al. (Cons.) as support of this recommendation, AIC contends they ignore the most recent Commission decision in Docket No. 11-0282.

With respect to MUT, AIC states the basis for Staff's recommendation appears to be the result of Mr. Kahle's interpretation of the filing instructions for the EAC. AIC notes the issues and filing instructions that Mr. Kahle discusses apply solely to the EAC, and Mr. Kahle provides no explanation as to why a revenue lag of zero days should be applied to the MUT. As Mr. Heintz explained, municipal taxes are paid on the last business day of the month for the previous month, and are paid on the due date in accordance with the municipal ordinances. AIC claims that its CWC calculation reflects its actual MUT remittance practice.

AIC notes that Mr. Brosch is the only witness to propose a zero revenue lag for the gross receipts taxes ("GRT"), which AIC states are not pass-through taxes. AIC notes Mr. Brosch provided no explanation as to why the GRT should be treated the same as pass-through taxes and thus, his recommendation should be rejected.

While Staff and IIEC contend that AIC provides no service related to pass-through taxes, AIC argues this is irrelevant to the net difference between the receipt of cash and the remittance of funds (in other words, the number of days AIC has access to the funds) on which AIC's lead-lag study is focused. AIC asserts that whether or not a service is provided, AIC must still bill, collect, and process the revenues associated with pass-through taxes. In advocating their (unbalanced, conceptual) zero-day revenue lag approach, AIC complains that Staff and AG/AARP also ignore that AIC's treatment of pass-through taxes in its CWC calculation is consistent with the Commission's Order in

AIC's most rate recent proceeding, Docket No. 11-0282. AIC opines that IIEC goes one step further, contending that Docket No. 11-0282 is inapposite because it was "based on exigencies of state government finances that no longer exist." AIC submits that this contention is unfounded, and a fair reading of the Order fails to support IIEC's position.

AIC recommends the Commission reject the parties' proposed zero days revenue lag attributed to pass-through taxes in favor of the 34.54 day revenue lag supported by AIC. AIC suggests its analysis accurately reflects the actual timing of the billing, collection, processing, and bank float associated with customers' payments during the test year.

ii. Staff Position

Staff recommends that the Commission not allow a revenue lag for pass-through taxes. Staff notes that pass-through taxes are not operating revenues and are not included in the revenue requirement as operating revenues, rather pass-through taxes are funds provided by ratepayers. Utilities are required to collect the pass-through taxes from ratepayers and remit the pass-through taxes to the taxing body within 20 to 30 days after collection from ratepayers. Because pass-through taxes are funded by ratepayers, Staff states the utility has no investment in pass-through taxes on which ratepayers should pay a return through increased CWC.

Staff claims that its position is consistent with the Commission's final Orders in both AIC's most recent electric rate case (Docket Nos. 09-0306 et al. (Cons.), April 29, 2010 Order at 54) and the only other formula rate case that has come before the Commission (Docket No. 11-0721, May 29, 2012 Order at 45) While AIC and ComEd do not operate in the same municipalities, Staff notes they both operate under the same State statutes for EACs, and suggest it would be unreasonable for a formula rate to incorporate a different lag for the same tax in a formula that should, for the most part, be consistent.

While AIC argues that its choice to remit pass-through taxes earlier than required justifies increasing CWC, Staff opines that ratepayers should not be burdened with higher rates because of AIC's business decision. Regardless of when AIC elects to remit the pass-through taxes, Staff notes the funds were provided by ratepayers, not investors, and ratepayers should not have to pay a return on funds not provided by investors.

Staff opines that AIC's argument that pass-through taxes are somehow transformed from taxes to operating revenue because they are collected through the same billing system used to collect utility service revenue, is incorrect. Staff argues that the method used to collect pass-through taxes does not change the fact that they are indeed ratepayer supplied funds.

Staff suggests that AIC witness Heintz could not even agree with AIC's logic, noting that he testified that AIC provides no service related to pass-through taxes, and admitted that AIC does not have a revenue lag for funds received for which no service was provided.

iii. IIEC Position

IIEC asserts that AIC's calculation of a revenue lag of 34.54 days for EAC is erroneous and unreasonable, noting that AIC is not required to remit EAC to the taxing authority until after AIC already has the monies in-hand from customers. IIEC suggests that AIC's decision to prepay its EAC remittances could be considered imprudent, and it is at the very least an unreasonable cost to pass on to the utility's ratepayers. In several prior cases, IIEC notes that the Commission ordered a zero-day revenue lag for pass-through taxes (including EAC), citing Docket Nos. 09-0306 et al. (Cons.), April 29, 2010 Order at 54-55; Docket No. 10-0467, May 24, 2011 Order at 48; and Docket No. 11-0721, May 29, 2012 Order at 41-42.

IIEC states that the Commission's exceptional treatment of EAC in AIC's most recent gas rate case, as testified to by Staff, was based on exigencies of state government finances that no longer exist. Even in that case, IIEC claims a root cause of the EAC CWC controversy was the decision by AIC to voluntarily remit taxes ahead of the date required by the taxing authority. In the circumstances of this case (with governmental exigencies removed), IIEC argues that AIC's questionable prepayment decision and its attempt to compel ratepayers to pay increased capital costs is unreasonable. IIEC urges the Commission to reject the resulting calculated CWC effect, and to deny recognition of any CWC requirement for AIC's EAC remittances.

IIEC opines that the zero revenue lag proposed by it and the other parties simply reflects the fact that AIC provides no EAC service for which it incurs out of pocket or cash expenses and notes that AIC acts as a conduit for EAC remittances. IIEC avers that AIC is only required to remit funds it has already collected, and AIC's voluntary early remittances do not engender prudent, reasonable CWC costs that should be recovered from ratepayers.

While AIC's delivery service rates recover its capital and operating costs of providing service to its customers, IIEC notes that AIC does not incur similar costs for EAC, since it provides no service in that connection. IIEC suggests that AIC witness Heintz confirmed that, in general, where the utility receives funds when there has been no service provided, there is no revenue lag, which IIEC argues is precisely the situation with respect to EAC, in that AIC is merely a conduit forwarding EAC to the appropriate taxing authority.

Even if one accepts AIC's contention that there is a revenue lag associated with pass-through taxes such as EAC, IIEC avers that AIC's calculation of the revenue lag period is flawed. As shown in IIEC Ex. 2.1, the Illinois Department of Revenue ("IDOR") Form RPU-6 instructions for remitting EAC repeatedly refer to collected revenues, and the instructions state plainly:

> You must file Form RPU-6 on or before the 20th day of the month to report and pay the total amount of assistance charges you collected from your customers during the preceding month.

Notwithstanding these instructions, IIEC claims that AIC made a management decision to base its remittances to IDOR on the amounts billed, rather than the amounts collected. IIEC suggests that AIC has reflected this management practice in its CWC calculation, thereby increasing its revenue requirement and ratepayers' rates.

IIEC argues that AIC's decision to make early remittances is not properly reflected in its expense lead determination. As AG/AARP witness Brosch confirmed, AIC's calculation of days the utility has collected EAC funds in its hands before remitting them to the taxing authority does not take account of actual customer payment behavior. IIEC contends that AIC begins its count of lead days at the end of its scheduled collection of timely payments on bills from the prior month – not when it begins receiving payments. IIEC notes that AIC assumes that payments are made only in the month following its billings, then uses its mid-point assumption to calculate that the utility holds EAC funds only from the midpoint or 15th of the month after bills go out until the 20th of that month, when remittances are due – a period of only 4 days (15th to 20th).

iv. AG/AARP Position

AG/AARP urge the Commission to correct AIC's recognition of the pass-through expenses to reflect a zero revenue lag day value associated with pass-through charges for EAC, MUT, and GRT. AG/AARP suggest this is necessary to reflect the fact that these taxes are completely ratepayer funded and have no CWC impact because the inflows and outflows earmarked for these taxes occur after taxable revenues have been collected by the utility. AG/AARP argue that AIC has made no showing that there is a need for CWC with respect to pass-through tax transactions, and notes that Staff concurs on this point and recommends Commission adoption of similar CWC adjustments.

AG/AARP assert that this proposed adjustment is also consistent with the Commission's finding in Docket Nos. 09-0306 et al. (Cons.), AIC's last completed rate case, which accepted Staff's position that pass-through taxes are completely funded by ratepayers, with the inflows and outflows earmarked for these taxes perfectly balanced. AG/AARP note that in Docket Nos. 09-0306 et al. (Cons.), Staff took issue with AIC's treatment of pass-through taxes in the calculation of the Revenue Collection Lag in AIC's lead/lag study. The Commission adopted Staff's adjustment to AIC's CWC proposal, stating:

> As an initial matter, the Commission accepts Staff's argument that the utility has no "investment" associated with pass-through taxes. Since every dollar for pass-through taxes is collected from the ratepayers, the inflows and outflows earmarked for these taxes should be perfectly

> balanced. Thus the need for CWC should not arise with respect to pass-through tax transactions. This conclusion is consistent with prior Commission decisions. Nicor Docket No. 08-0363 at 11-12. Staff distinguishes pass-through taxes from other cash flows in that, unlike other revenue, pass-through taxes are not directly associated with the provision of utility service. The Commission believes that Staff makes a legitimate point here. The Company would have us believe there is an additional and measurable cost to pass-through taxes but fails to illustrate how a tax that is completely ratepayer-funded could generate any costs or expense. This is simply not the case. The Commission finds that Staff's proposed adjustment to the CWC requirement must be accepted. (Docket Nos. 09-0306 et al. (Cons.), May 6, 2010 Order at 54)

More recently, AG/AARP note that the Commission found in ComEd Docket No. 10-0467 that pass-through taxes should not be assigned a revenue lag because they are payable after revenues are collected from customers. There, the Commission noted:

> The Commission agrees with Staff's interpretation as to the EAC/REC and GRT/MUT tax issues. For the EAC/REC tax, the utility shall remit all moneys received as payment to the Illinois Department of Revenue by the 20th day of the month following the month of collection. Under the GRT/MUT tax, this ordinance requires ComEd to file a monthly tax return to accompany the remittance of such taxes, due by the last day of the month following the month during which such tax is collected. Both the statute and ordinance requires ComEd to remit these pass-through taxes after they have been collected from customers. ComEd stated in its briefs that the Company correctly pays these taxes in the month following activity that occurs in a prior "tax liability" month. The Commission concludes that the CWC calculation for GRT/MUT pass-through taxes should reflect zero revenue lag days and 44.21 expense lead days and zero revenue lag days and 35.21 expense lead days for EAC/REC pass-through taxes as supported by Staff. (Docket No. 10-0467, May 24, 2011 Order at 48)

While AIC cites the Commission's Order in Docket No. 11-0282 as support for their position, AG/AARP note the Commission has specifically addressed the issue of how to treat the collection revenue lag associated with these pass-through taxes as recently as a few months ago in ComEd's formula rate docket, Docket No. 11-0721. There the Commission concurred with Staff and intervenor proposals (including AG/AARP) that set the revenue collection lag for these pass-through taxes at zero, finding:

> The Commission agrees with Staff and the intervenors' proposal to use zero revenue lag days for EAC/REC and GRT/MUT. This was also the decision of this Commission in the Company's prior docket, Docket 10-

> 0467. The Commission notes that ComEd's process for collecting and remitting pass-through taxes has not changed since Docket 10-0467. The Commission finds that pass-through taxes should not be assigned a revenue lag because they are payable after revenues are collected from customers. ComEd's decision to pay the subject taxes and charges before they are due should not require its customers to pay the increased costs associated with increased cash working capital requirements. (Docket No. 11-0721, May 29, 2012 Order at 45-46)

AG/AARP allege the adjustments recognized in Mr. Brosch's recalculation of the AIC CWC allowance has the effect of eliminating the revenue lag day values for these pass-through amounts, and would be consistent with prior Commission orders. IIEC notes that both Staff witness Kahle and IIEC witness Rackers proposed similar adjustments.

Consistent with these adjustments, Mr. Brosch also revised the expense lead day value for the EAC because Illinois law provides that a public utility engaged in the delivery of electricity shall assess each of its customer accounts a monthly charge and shall remit all moneys received as payment to the IDOR by the 20th day of the month following the month of collection, which terms yield an expense lead days value of 20 days, plus half of the prior month of 15.2 days, for a total expense lead of 35.2 days.

AG/AARP note that AIC objected to Staff and IIEC's proposed pass-through tax adjustments to the CWC calculation, as well as to AG/AARP's. While AIC claims that it has had a long-standing practice of remitting pass-through taxes based upon monthly billings adjusted for write offs, and the time and resources that would be required to modify systems to file the reports on an alternative date justify retention of the filing dates and CWC requirement calculation assigned to these pass-through taxes, AG/AARP aver that Staff recognizes that AIC chooses to remit pass-through taxes earlier than State statutes and municipal ordinances require. AG/AARP assert that the result is a net revenue collection lead that is understated by the difference between the date AIC remits pass-through taxes and the date AIC is required to remit pass-through taxes, which results in a higher CWC requirement than should be approved.

AG/AARP recommend that the Commission adopt the necessary adjustments to remove the revenue lag assigned to the aforementioned pass-through taxes in the calculation of AIC's CWC requirement.

v. CUB Position

CUB suggests that the adjustment of AG/AARP witness Brosch and Staff witness Kahle to use zero revenue lag days for pass-through taxes for EAC, MUT, and GRT is appropriate and necessary and should be adopted by the Commission. CUB argues this proposed adjustment is consistent with the recent ComEd Order, Docket No. 11-0721, where the Commission found that "pass-through taxes should not be assigned a revenue lag because they are payable after revenues are collected from customers."

CUB notes the Commission also held that a utility's "decision to pay the subject taxes and charges before they are due should not require its customers to pay the increased costs associated with the increased cash working capital requirements." CUB submits that this decision was also consistent with the Commission decisions in Docket Nos. 09-0306 et al. (Cons.) and 10-0467. CUB suggests the same analysis and conclusion is appropriate here, and that the Commission should reject AIC's proposed CWC calculation and adopt the adjustment proposed by AG/AARP and Staff.

vi. Commission Conclusion

The Commission notes that AIC is proposing a revenue lag of 34.54 days for pass-through taxes, specifically its EAC and MUT in relation to its CWC calculation. AIC suggests that this finding would be in accordance with the Commission's finding in Docket No. 11-0282, asserting that nothing has changed in AIC's handling of these pass-through taxes since Docket No. 11-0282 was decided by the Commission.

Staff, IIEC, AG/AARP, and CUB, however, argue that the proper revenue lag for these items is zero days, as these pass-through taxes are not operating revenues and are not included in the revenue requirement as operating revenues, but rather are funds provided by ratepayers. These parties also note that a finding of zero lag days would be consistent with the Commission's decision in the ComEd formula rate docket, Docket No. 11-0721. Staff and the other parties also contend that AIC is paying these funds in question earlier than required, and complain that ratepayers should not be forced to suffer the consequences of AIC's actions.

The Commission agrees with Staff and the other parties that the proper revenue lag associated with these items should be zero days. The Commission recognizes that in Docket No. 11-0282 it had granted AIC revenue lag days in its CWC calculation for these items, and indicated that it would revisit this issue if AIC changed the manner in which it handled these items. The Commission also recognizes that in ComEd's formula rate case, in addressing this same issue, the revenue lag days were set at zero, despite ComEd's reliance on Docket No. 11-0282. The Commission believes that consistency between the relevant utilities in the smart grid dockets is an important consideration to take into account. The Commission therefore finds that the appropriate revenue lag days for this issue should be zero, as recommended by Staff, IIEC, AG/AARP, and CUB.

b. Revenue Collection Lag

i. AIC Position

AIC states that a key component of the CWC calculation is the revenue lag, which measures the elapsed time between the delivery of AIC's product (i.e., electricity) and its ability to use the funds received as payment for the delivery of the product. AIC notes that one component of the revenue lag is the collection lag, which is the average amount of time customers take to pay their utility bills after the bills are mailed. For the purposes of determining its CWC requirements, AIC calculated the collection lag using an analysis of actual aged receivables data from AIC's Customer Service System. The weighted aged receivables for the twelve months ended September 30, 2010 were then adjusted to reflect potentially uncollectible receivables, which resulted in an average collection lag of 30.67 days. AIC asserts that use of this aged receivables methodology was recently approved for AIC in Docket Nos. 09-0306 et al. (Cons.), where the Commission agreed that the actual weighted-average number of collection days should be used in the determination of CWC costs. (Docket Nos. 09-0306 et al. (Cons.), November 4, 2010 Order on Rehearing at 56)

AIC notes that IIEC and AG/AARP instead recommend that the Commission not utilize AIC's actual aged receivable methodology, and instead, they recommend a collection lag of 21 days and 22.04 days, respectively. AIC recommends that the Commission reject IIEC's arbitrary collection lag calculation, in favor of AIC's calculations. AIC notes that despite AIC's use of actual calculated collection lags, IIEC witness Rackers asserts the Commission should use the 21-day collection lag based on the payment periods specified in 83 Ill. Adm. Code 280.90. AIC suggests however, that the 21-day lag suggested by Mr. Rackers is an arbitrary lag amount. AIC claims that the Commission, in rehearing on Docket Nos. 09-0306 et al. (Cons.), found that it is appropriate to use actual collection lag information to determine CWC requirements. AIC notes that in Docket No. 11-0282, AIC's most recent gas rate case, the Commission accepted AIC's proposed collection lag of 30.67 days, based on the same actual aged receivables methodology AIC uses in this proceeding. (Docket No. 11-0282, January 10, 2012 Order at 13-14) AIC notes that Staff agrees with AIC's proposed collection lag calculation.

AIC states that Section 280.90(c) establishes only that the number of days between the date the bill is postmarked and the due date for payment of the bill must not be less than 21-days; however AIC notes this rule does not establish or reflect the actual payment date of AIC's customers. AIC notes that Mr. Rackers admits that the 21-day collection lag is nothing but a proxy for a properly calculated collection lag. The 21-day collection period recommended by Mr. Rackers, by contrast, is not an average of any payment data, nor does it reflect any real or measured customer payment pattern. Mr. Rackers has provided no study, analysis, actual data, or other empirical evidence that supports the conclusion that the 21-day period is representative of AIC's customers' payment patterns. As Mr. Rackers admits, it fails to account for the additional two-day grace period, provided for by the Commission's rules, before late fees can be assessed for mailed payments, and the effect of that grace period on customer payment practices. AIC asserts that an arbitrary substitution, such as the 21 days suggests, is not needed because AIC has prepared a lead-lag study in this case that provides actual calculated collection lags based on actual customer payments.

AIC also argues that AG/AARP's modification to AIC's methodology should be rejected, noting that AG/AARP witness Brosch recommends AIC's collection lag be revised to insert grace period assumptions as were used in ComEd's calculations which were approved by the Commission in Docket No. 10-0467. AIC notes however, that Mr.

Brosch admits that while the ComEd grace period assumptions are arbitrary, he still suggests the application of the grace period to modify the midpoints used in AIC's aged accounts receivable analysis. AIC opines that Mr. Brosch takes exception to AIC's use of aged accounts receivables to calculate collection lag on one hand, yet relies upon an aged receivables analysis, with an adjustment, to arrive at his proposed collection lag.

AIC complains that the record in this proceeding provides no evidence that the adjustment proposed by ComEd has any applicability to AIC or its customers' payment patterns. Moreover, AIC notes it has used a collection lag methodology which is based on actual data, and which method has been repeatedly sanctioned by the Commission and similar to that employed by other major Illinois utilities. In addition to being based on actual data, AIC argues that its collection lag is in line with those approved for other Illinois utilities by the Commission. In fact, even with the use of the suggested grace periods; AIC notes that its collection lag is less than that approved in either of ComEd's last two rate cases, Docket Nos. 10-0467 and 11-0721.

AIC further notes that Mr. Brosch also proposes that in future rate proceedings, AIC should be required to calculate the collections lag based upon what he deems to be generally accepted methods: (1) a study of the timing of customers' actual remittances; or (2) daily accounts receivable turnover. AIC suggests these proposals should be rejected as unnecessary. AIC urges that a customer remittance analysis to calculate the collections lag should not be used, stating that as the name implies, the customer remittance analysis examines the timing of actual payments made by customers. While on its face, the analysis would seem reasonable; it would exclude any customer bills that have not been paid. AIC avers that this analysis is biased towards customers that pay their bills on time and either ignores or penalizes AIC for those customers that have outstanding balances. AIC states further that the additional studies proposed by Mr. Brosch would result in additional cost, however it has not been shown that undertakings such studies would produce a materially better result.

ii. Staff Position

Staff recommends that the Commission not set the revenue collection lag at 21 days as proposed by IIEC. Staff notes that 83 Ill. Adm. Code 735.160(a)(2) establishes that the number of days between the date the utility customer receives the bill and the due date for payment of the bill must not be less than 21 days. Staff however, argues that this rule does not reflect the actual collection lag which has been calculated by AIC in a lead/lag study in a manner consistently accepted by the Commission, indicating that Staff supports the collection lag days as proposed by AIC.

iii. IIEC Position

IIEC argues that AIC's proposed collection lag component of its CWC calculation is excessive. IIEC notes that AIC's CWC study calculates the utility's revenue lag as 30.67 days, while IIEC proposes a revenue lag of 21 days. IIEC states that its proposal is not the result of a separate CWC study, but rather, it is a reason-based surrogate for the results of AIC's flawed CWC study, a study that rests on unsupported assumptions, lacks empirical validation, and implies that (as a group) AIC's customers pay their bills well after their 21-day due date. IIEC argues that AIC's study results are not reasonable and lack record support.

To support its study, IIEC notes that AIC relies mainly on the Commission's acceptance of the so-called "midpoint assumption," which posits that the midpoints of monthly utility payment periods are valid substitutes for empirical data on the timing and amounts of customer payments. IIEC states that AIC witness Heintz explained that "the midpoint methodology presumes that payments occur ratably over the course of a month." IIEC notes however, that AIC acknowledges that its expert undertook no investigation to test whether the fundamental assumption underlying its CWC calculations actually bears any resemblance whatsoever to how AIC's customers actually pay their bills. IIEC notes that Mr. Heintz acknowledges that a deviation from the midpoint of the month would produce a different collection lag, and he concedes that he did not conduct an analysis where payments occur ratably over the course of a month.

IIEC states the Commission has accepted that assumption in several earlier cases where utilities claimed a lack of utility-specific payment distribution data, however IIEC suggests that the practice of accepting these assumptions is no longer reasonable. In fact, it appears to IIEC that the Commission's past orders are one reason AIC made no effort to validate or to replace that foundational assumption, though a completed investigation or study could eliminate the need for such assumptions.

IIEC's proposal is based on the provisions of 83 Ill. Adm. Code Section 280.90, which gives residential customers 21 days to pay their utility bills; before late fees may apply, and commercial, industrial and government agencies have only 14 days. IIEC suggests that its proposed 21-day collection lag reflects an average period of time, with some customers paying before and others after 21 days. IIEC notes that costs associated with late paying customers that are not considered in late fees are included in the billing and collection expenses, and since all these costs are being reflected in the calculation of rates, there is no need to include any additional adjustment to capture these costs. IIEC argues that AIC's ratable payment assumption means a significant number of customers must pay in less than 21 days, therefore IIEC's proposed 21-day collection lag is a conservative estimate that is favorable to the utility.

IIEC notes that AIC does not deny that the 21 day payment period, in fact, does affect customer payment behavior. IIEC states there are meaningful consequences associated with not paying by the due date, such as late fees, negative impact on credit history, and impairment of future dealings with the utility. IIEC suggests the Commission's payment rule provides a reasonable measure to use as a replacement for an AIC CWC calculation that continues to be based on assumed customer payment behavior that has never been validated.

iv. AG/AARP Position

AG/AARP note that in the order in AIC's last electric and gas rate order, Docket Nos. 09-0306 et al. (Cons.), the Commission rejected AIC's proposed revenue lag, with the following explanation:

> The Commission has concerns about AIU's proposed method for calculating the CWC requirement. The Commission understands that IIEC's reason for proposing 21 lag days is that it is the maximum lawful period customers can delay payment. Section 285.2070 of Part 285 specifically contemplates the use of a lead/lag study. AIU presented a detailed lead/lag study using methods that have been adopted by the Commission in numerous previous proceedings, but AIU assumed, rather than proved, the collection lag periods used in its study. The absence of empirical evidence supporting the collection lag assumptions used in Ameren's lead/lag study weighs against the utility, which has the burden of proof in this proceeding. Under these circumstances, IIEC's proposal to use a 21 day collection lag in calculating the CWC requirement is hereby adopted. (Docket Nos. 09-0306 et al. (Cons.), May 6, 2010 Order at 54)

In its Order on Rehearing issued November 4, 2010, AG/AARP state the Commission revised its decision regarding the revenue collection lag day after concerns were raised by AIC regarding the inclusion of significant amounts of late fee revenues while the Commission-approved revenue collection lag assumed customers' remittances fell generally within the Commission's 21-day payment rules:

> While the evidence and arguments on Rehearing are not what the Commission anticipated, they are helpful in considering the issue of CWC and the Commission appreciates the input of the parties. It appears that no party disputes AIU's estimate of the revenue it receives in late payment fees. While IIEC disputes that AIU incurs a cost associated with late payments, it does not appear to contest the method for quantification offered by AIU. The Commission's review of the record indicates that AIU actually has collected revenues associated with late payments. The fact that AIU collects late fees suggests that some customers pay their bills after the dates specified in the Commission's rules. If all customers paid their bills by the time specified in the Commission rules, it would not be possible for AIU to collect late fees.
>
> IIEC argues there is no connection between the amount of late fees collected and AIU's estimate of the capital costs associated with late payments. The Commission believes, however, that inherently, if a customer does not pay its bill in a timely manner, it will be necessary for a utility to finance its operations in interim with an alternate source of capital. This is the entire reason for a CWC allowance and a lead/lag study.

> The Commission is of the opinion that the methodology espoused by AIU and Staff is the most appropriate for calculating AIU's CWC allowance in this instance. The position of AIU, as adopted by Staff, persuasively shows the effect of the late fee revenue on AIU's capital costs, and as such it will be adopted by the Commission on Rehearing. (Docket Nos. 09-0306 et al. (Cons.), November 4, 2010 Order on Rehearing at 56)

AG/AARP contend this historical perspective regarding lead lag study issues is important, because in its formula rate calculations, AIC is again employing the same form of revenue collection lag calculations used in Docket Nos. 09-0306 et al. (Cons.), under which AIC has assumed, rather than proven, dates when customers, on average, actually remit payments of their utility bills.

AG/AARP note that Mr. Brosch explained that the revenue lag is the single most important lag value in a study of CWC, because it is applied to the largest amount of dollars. Mr. Brosch testified that he documented a number of problems with AIC's method of calculation to estimate the revenue collection lag, all of which are similar to the problems he noted in the recent ComEd formula rate case, Docket No. 11-0721. AG/AARP note that AIC, as well as other Illinois utilities, have adopted a shortcut method to estimate the revenue collection lag, in place of more traditionally used methods that more accurately quantify this important lead lag study value.

As explained by Mr. Brosch, since lead lag studies first emerged in the 1980s as the preferred and most accurate approach to quantify CWC, measurement of the revenue collection lag has most frequently been quantified using either a statistical sampling of actual customer remittances or a calculation of daily average Accounts Receivable "turnover" ratios that indicate the average number of days of revenues outstanding calculation. AG/AARP state that Mr. Brosch testified that the Commission's recent, repeated acceptance of the utilities' unsubstantiated assumptions about when customer payments are received is an arbitrary methodology not commonly used in the states in which he has testified. AG/AARP suggest that either of the alternative, more precise methods mentioned can produce reasonable estimates of how quickly utility customers actually pay their bills and have received widespread acceptance among regulators. However, either as a result of limited data availability and/or an interest in overstating revenue collection lags, AG/AARP note that Illinois utilities have achieved some success convincing the Commission that arbitrary mid-point remittance assumptions applied to broad categories of aged receivables can achieve a reasonable result. AG/AARP, however, urge the Commission to revisit this issue based on the evidence of this record and order AIC to improve upon the accuracy of revenue collection lag quantification to ensure that ratepayers are not paying excessive rates. Requiring AIC to revisit its CWC estimation methodology is essential AG/AARP argue, because AIC now proposes to retain these assumptions and not re-visit its CWC needs for a three-year period under formula rate regulation.

AG/AARP note that AIC's revenue lag is comprised of five segments, including:

1. A customer usage or service period lag of 15.21 days, plus
2. An average billing period lag of 1.51 days, plus
3. A collection lag between the billing date and customer remittances estimated at 30.67 days by AIC, plus
4. A payment processing lag of 1.39 days for processing and depositing of remittances, plus
5. A bank float of 0.97 days until deposited funds are available for use by AIC.

AG/AARP suggest that the Commission has recognized in previous rate orders that there are major problems with the third element of AIC's calculation that must be corrected. AG/AARP urge that AIC be required to undertake a systematic study of the timing of customers' actual remittances to more accurately estimate its revenue collection lag; using either of the two generally accepted methods used in other regulatory jurisdictions that employ lead lag studies. AG/AARP note that Mr. Brosch testified that until improvements are made in this area, AIC's lead/lag study is hopelessly inaccurate and should not be relied upon in any future formula ratemaking process.

AG/AARP opine that the revenue collection lag underlying AIC's proposed CWC amounts was estimated by AIC witness Heintz through the application of very crude assumptions to quite broad "aged" categories of month-end accounts receivable balances. AG/AARP note that Mr. Heintz admitted he has not actually measured how long it takes to collect revenues from AIC customers, but that instead he looks to a breakdown of the recorded week-end Accounts Receivable balances by customer class and assigns, without any supporting analysis, arbitrarily assumed revenue collection dates to each grouping of aged receivable balances.

AG/AARP state that Mr. Heintz, for example, estimated that every one of the thousands of residential customer accounts with balances ages that ranged from 0 to 30 days old were arbitrarily assumed to be remitted precisely on day 15; while accounts ranging from 31 to 60 days old were assumed to be remitted precisely at the mid-point of this period, on day 45, and all residential customer accounts with balances 61 to 90 days old are assumed to be fully paid to AIC precisely on day 75, which is again the mathematical mid-point of the period. AG/AARP note that for all customer account balances more than 90 days old, a statistically impossible average age of 90 days was assumed by Mr. Heintz in place of an alternative mid-point assumption.

AG /AARP note that a similar midpoint methodology was challenged as it was employed by ComEd in Docket No. 10-0467 and in Docket No. 11-0721; however ComEd did attempt to limit the financial impact of some of the gross inaccuracies arising from the utilization of arbitrary Accounts Receivable aging mid-point assumptions. As noted by Mr. Brosch, ComEd applied certain "grace period" assumptions to the youngest aging categories in an effort to introduce conservatism into the otherwise unsupportable mid-point assumptions that were applied to aged accounts receivables. AG/AARP note that for example, because residential customers have 20 days before their unpaid utility bills are delinquent, ComEd assigned an assumed zero-lag value to all residential balances 0-30 days old, and assigned an eight-day assumed remittance date to its small and large commercial accounts falling within the same aging category because of payment due date terms in Commission rules. AG/AARP opine that these changes did not remedy the inherent inaccuracy caused by using unproven mid-point assumptions applied to each Accounts Receivable aging category, but they did produce a result for ComEd that was somewhat more credible than could be calculated without injecting these additional assumptions regarding grace periods.

AG/AARP suggest that more conservative assumptions, if applied by Mr. Heintz within the AIC lead lag study, would produce significantly different CWC results, however Mr. Heintz has completely ignored the payment due date grace periods that customers have to pay their bills. Additionally, AG/AARP note that the AIC study does not exclude accounts receivable amounts over 365 days old or the amounts related to inactive accounts, yet another reason why the AIC asserted CWC value is overstated.

Notwithstanding the flawed midpoint assumption methodology used by Mr. Heintz, AG/AARP recommend at this time, and only for initial determination of the inception rates that will later be subject to reconciliation, that AIC's proposed lead lag study be modified to incorporate revision of AIC's estimated revenue collection lag to insert reasonable grace period assumptions, as were used in ComEd's calculations approved by the Commission in Docket No. 10-0467, so as to provide conservatism and recognition of the period within which residential and commercial customers' bills are payable but not delinquent. AG/AARP state that Mr. Brosch, using these changes, retained all of AIC's other arbitrary assumptions and methods in estimating the revenue collection lag calculations, and calculated a revised overall revenue lag of 41.12 days.

AG/AARP aver that the CWC impact of revising AIC's collection lag and overall revenue lag for the effects of billing grace periods, using ComEd's methodology, is significant, noting that the collection lag component of the revenue lag changes from 30.67 days in AIC's study to 22.04 days using the ComEd grace period assumptions. AG/AARP state that this 8.63 reduction in collection lag days results in a revised overall revenue lag of 41.12 days, compared to AIC's proposed 49.75-day revenue lag. AG/AARP contend that the overall impact upon CWC included in rate base from a 8.63-day reduction in the revenue lag is approximately $13.2 million less CWC in rate base, and AG/AARP recommend that this revision should be adopted by the Commission.

While AIC complains that these grace period assumptions are imposing an adjustment for another company on AIC and that there is no evidence that the grace period assumptions are applicable to AIC customer payment patterns, AG/AARP suggest that AIC has missed the point of the assumptions. AG/AARP note that the insertion of grace period assumptions simply recognizes that due date grace periods that are specified in the Commission's rules should be considered in formulation of the assumptions applied to aged receivables, and argue that these grace periods apply to all utilities under Commission rules, and must be recognized, particularly since AIC presented no data or analysis of its customer payment patterns. AG/AARP also contend that AIC is here recommending an inexplicably higher revenue lag days calculation in Illinois than has been proposed or adopted for its sister utility operation in Missouri. While AIC defends its analysis by showing that the Commission has adopted the midpoint aging interval approach in other major utility rate cases, AG/AARP respond that they have compared AIC's results to non-AIC utilities outside of Illinois as a test of reasonableness, and the results showed that AIC's proposed revenue lag was excessive.

AG/AARP assert that the revised revenue lag day value resulting from the inclusion of grace period assumptions will significantly improve the reasonableness of AIC's study, by injecting conservatism into the results produced by AIC's inherently imprecise and arbitrary mid-point assumptions, causing the resulting revenue lag to be more consistent with the results of other large utilities outside of Illinois. However, AG/AARP contend that an actual measurement of the revenue collection lag should be required of AIC in the future. In order to more precisely correct AIC's estimated revenue collection lag day value and ensure that ratepayers are not overpaying for utility service, AG/AARP suggest that AIC be required to conduct statistical samples of actual customer remittances, to determine the average number of days between collection date and the related prior billing date(s). Alternatively, AIC should be required to collect and analyze its average daily electric service accounts receivables balance, net of the related uncollectibles reserve, to quantify how many days of its sales are "outstanding" within these balances.

Mr. Brosch explained that this Accounts Receivables "turnover" calculation relies upon dividing the net average daily balance of Accounts Receivables by annual utility sales revenues and is routinely used in other jurisdictions to quantify the revenue collection lag for energy utilities. AG/AARP suggest that AIC should be required to employ either or both of these methods in future lead lag studies to actually measure customer remittance patterns and more accurately quantify the revenue collection lag, before any future CWC amounts are included in rate base.

In response to the proposal that AIC actually study and measure customer payment patterns, Mr. Heintz claims that there is bias towards customers that pay their bills on time and ignores (or penalizes AIC for) those customers who have outstanding balances. AG/AARP suggest that there is no bias in studying the timing of actual customer payments to quantify the revenue lag, and that a reasonable sample of customers' remittances would not be biased toward customers who pay their bills on time, because the sample would also capture payments made late, if properly designed and conducted. AG/AARP contend there also is no "penalty" associated with customers having outstanding balances, because all accounts receivable are ultimately either paid by customers or become uncollectible, and utility rates are set based upon a revenue requirement inclusive of uncollectible expenses.

While Mr. Heintz also complained that he is unaware of any “preferred and most accurate approach” to lead/lag study analysis, AG/AARP suggest that Mr. Brosch’s rebuttal testimony provides a detailed discussion of the daily accounts receivable turnover approach and the sampling of customers’ remittance approaches in AG/AARP Ex. 3.4. AG/AARP claim that these methodologies are routinely applied by other utilities in CWC presentations that Mr. Brosch has observed and reviewed in other proceedings throughout the country. AG/AARP opine that it is important that the Commission order AIC to utilize a CWC analysis methodology that balances both AIC’s and ratepayer financial interests, since with the new formula ratemaking AIC will be resetting its rates each year, this shift in regulatory rate-setting justifies requiring the utility to conduct its CWC needs in a more reliable way than simply utilizing a midpoint aging interval methodology.

AG/AARP note that AIC claims in its Initial Brief, that it had performed an analysis of actual aged receivables data, implying that AIC examined the actual customer receivables and remittances to calculate the average amount of time for the Revenue Collection lag. AG/AARP contend that AIC actually did not perform such an analysis, with Mr. Brosch explaining that AIC actually used a random, arbitrary midpoint methodology that applies crude assumptions to quite broad “aged” categories of month-end accounts receivable balances.

AG/AARP recommend that, for purposes of setting rates in this docket, the Commission should adopt Mr. Brosch’s 41.12 days revenue lag number, based upon accounts receivable aging midpoints with the same grace period assumptions that were approved for ComEd in Docket Nos. 10-0467 and 11-0721. AG/AARP note that customer remittance due dates pursuant to the Commission’s rules are the same for AIC and ComEd, and AIC has provided no justification for deviation from this previously approved methodology. AG/AARP also suggest the Commission order AIC to either conduct a daily accounts receivable turnover analysis or use a statistically valid sample of customers’ actual remittances, for use in supporting AIC’s revenue collection lag day value within its next presentation of CWC needs in its 2013 formula rate filing.

v. CUB Position

In order to calculate its revenue lag, CUB notes that AIC has assumed, rather than proven, dates when customers, on average, actually remit payments of their utility bills. CUB suggests that this “shortcut method” of estimating the revenue collection lag should not be used in place of more traditionally used methods, which more accurately quantify this significant lead lag study value.

CUB notes that AIC employed a midpoint methodology of calculating the revenue collection lag, using what CUB characterizes as crude assumptions and broad “aged” categories of month-end accounts receivable balances. Rather than actually measuring how long it takes to collect revenues from its customers, CUB states that AIC assigned assumed revenue collection dates to groupings of aged receivable balances. The midpoint methodology of calculating the revenue collection lag is arbitrary, and though it has been accepted by the Commission in several recent cases, should be revisited to avoid potential misstatement of AIC's CWC requirement. CUB agrees with Mr. Brosch's recommendations for this case, along with his recommendation that in future reconciliations, beginning with the reconciliation of 2012 revenue requirements in AIC's May 2013 filing, AIC should be ordered to conduct a more extensive analysis of its actual revenue collection lag days.

vi. Commission Conclusion

The Commission notes that AIC has proposed a revenue collection lag of 30.67 days, indicating that it calculated the collection lag using an analysis of actual aged receivables data, which was then adjusted to reflect potentially uncollectible receivables. AIC contends that the method it used in this docket is the same method approved by the Commission in Docket Nos. 09-0306 et al. (Cons.). AIC objects to the methodology proposed by AG/AARP, noting that the record in this proceeding provides no evidence that the adjustment proposed by ComEd in its docket has any applicability to AIC or its customers' payment patterns. AIC also recommends that the Commission not accept AG/AARP's recommendation for future proceedings, contending that the analysis would be biased toward customers that pay on time and either ignores or penalizes AIC for customers that have outstanding balances. AIC also suggests that this proposal would entail additional costs, without any showing that it would produce a materially better result. AIC recognizes that Staff supports AIC's calculation on this issue, and urges the rejection of IIEC's suggested 21-day revenue collection lag, which is based on Section 280.90 of the Commission's rules.

As noted, IIEC recommends the Commission set a revenue collection lag based on the provisions of Section 280.90, which gives residential customers 21 days to pay their utility bills before late fees may apply while commercial, industrial, and government agencies have only 14 days. IIEC suggests that its proposed 21-day collection lag reflects an average period of time, with some customers paying before and others after 21 days.

AG/AARP complain that AIC is assuming, rather than proving, the dates on which customers actually paid their bills, therefore AG/AARP suggest that AIC's calculation is lacking. AG/AARP propose that AIC's lead lag study be modified to incorporate revision of AIC's estimated revenue collection lag to insert reasonable grace period assumptions, as were used in ComEd's calculations approved by the Commission in Docket No. 10-0467. AG/AARP contend that the impact of revising AIC's collection lag and overall revenue lag for the effects of billing grace periods, using ComEd's methodology, is significant. AG/AARP state that the collection lag of 30.67 days in AIC's study would be reduced from 30.67 to 22.04 using the ComEd assumptions. AG/AARP contend this would result in a revised overall revenue lag of 41.12 days, as compared to AIC's proposed 49.75 day revenue lag. AG/AARP also recommend that the Commission order AIC to either conduct a daily accounts receivable turnover analysis or use a statistically valid sample of customers' actual remittances in future filings. CUB supports AG/AARP's recommendation.

The Commission believes that the evidence presented shows that AIC has appropriately calculated the revenue collection lag; therefore it will be adopted for this proceeding. The Commission agrees with AIC that it has adequately considered the issues presented in calculating the collection lag, and the method used is the same as that accepted by the Commission in Docket Nos. 09-0306 et al. (Cons.). The Commission also will decline to accept the recommendation of AG/AARP for AIC in future proceedings to either conduct a daily accounts receivable turnover analysis or use a statistically valid sample of customers' actual remittances in future filings. The Commission agrees with AIC that the proposed method could be biased toward certain customers and unduly penalize AIC, without any evidence that the additional cost would produce a better result for the Commission's consideration.

c. Income Tax Lead and Lag

i. AIC Position

Consistent with Commission practice of not considering current and deferred income taxes separately for the purposes of calculating CWC, AIC states that it utilized statutory tax rates and payment dates when determining CWC. AIC notes that the Commission has a long-standing practice of setting AIC’s income tax expense based on statutory tax rates and payment dates when calculating income tax expense for revenue requirement purposes. As such, AIC notes it does not distinguish between current and deferred tax expense for CWC purposes, nor does AIC include permanent tax differences in its income tax expense calculation.

AIC recognizes that AG/AARP witness Brosch recommends revenue lag and expense lead days be set at zero for income taxes in calculating CWC because AIC’s 2010 income taxes currently payable are substantially negative and more than 100% of AIC’s 2010 income taxes are actually non-cash deferred income taxes, for which there is no current period cash flow that could contribute to CWC.

AIC complains that Mr. Brosch’s recommendation is not valid for setting AIC rates as it is not only inconsistent with Commission practice, it disrupts the balance between the ratemaking cost of service and the inputs to the CWC calculation. AIC notes the differentiation between current and deferred income tax expenses can swing between rate filings, reflecting then current tax laws, and assert that the use of statutory tax rates and payment dates maintains a consistent treatment of income tax expense for ratemaking purposes and avoids such swings in balances. AIC notes that both the Commission and Staff have accepted AIC’s calculation of income tax expense based upon the statutory tax rates and payment dates in prior rate proceedings. AIC notes that Mr. Brosch agrees with the use of statutory tax rates and payment dates in the calculation of CWC, therefore AIC suggests that his proposed adjustment to reflect zero days for the revenue lag and expense lead associated with income tax expense should be rejected.

While Mr. Brosch claims that income tax expense can be stated using statutory rates in the calculation of revenue requirement and at the same time use a different calculation for CWC; AIC avers that this is not a valid, consistent, or workable alternative in the setting of electric delivery service rates. AIC notes that the two methods are not consistent and produce different results, stating that a calculation of current vs. deferred income tax expense for AIC will produce a larger amount of income tax expense than use of statutory rates. As with any other operating cost of service, AIC suggests the levels of income tax expense included in CWC need to align with the level of such costs included in the calculation of revenue requirement, otherwise, the two calculations will not create a proper balance between the ratemaking cost of service and the inputs to the CWC calculation. Furthermore, AIC claims that the fact that it may not have a cash outlay in 2010 for current income taxes does not imply that the same will continue with future formula rate filings. AIC notes that Mr. Brosch does not offer a workable alternative for future rate filings when AIC will have a current income tax cash outlay.

While Mr. Brosch also cites to ComEd’s formula rate case, Docket No. 11-0721, as support for his recommendation, AIC opines that ComEd calculates income tax expenses based on actual rather than statutory rates; accordingly, citing to ComEd is not valid where the two methodologies are not aligned. For that and the other reasons above, AIC recommends that Mr. Brosch's proposed adjustment to income tax expense in the calculation of CWC should be rejected.

ii. Staff Position

Staff recommends that the Commission not set AIC's income tax lead and lag days to zero as proposed by AG/AARP witness Brosch. Staff considers the Commission to have a long standing practice of not considering current and deferred income taxes separately. Staff suggests that both Staff’s and AIC’s treatment of deferred income taxes for CWC is consistent with Commission practice.

iii. AG/AARP Position

AG/AARP suggest that a flaw in AIC's CWC presentation relates to its application of revenue and expense lead/lag calculations to about $77 million of Income Tax expenses, as if such amounts represent cash transactions. AG/AARP note that in the test year, more than 100% of AIC income taxes are “deferred” taxes, largely because of sizable income tax deductions being taken for bonus tax depreciation. AG/AARP state that per AIC Schedule C-5a, test year recorded income tax expense of approximately $66 million consists of about $116 million of deferred income tax expense and about $50 million of negative current income tax expense, such that after all of AIC’s proposed ratemaking adjustments and its proposed revenue reduction, adjusted currently payable income tax expense remains substantially negative. AG/AARP state that the breakdown of income tax expenses between the amounts that are deferred versus currently payable is very important in determining CWC, because deferred income tax expense represents a non-cash accrual for taxes that are expected to become payable in future years, while only the “currently payable” income tax expenses are cash costs that are relevant in determining CWC.

To correct this error, AG/AARP witness Brosch sets the revenue lag days and Expense Lead Day values to zero, asserting that because test year adjusted income taxes currently payable are substantially negative, it is inappropriate to assign any CWC to this expense. AG/AARP argue that more than 100% of AIC test year income taxes are actually non-cash deferred income taxes, for which there is no current period cash flow that could contribute to CWC, and it is essential that no lead/lag values be applied to this non-cash expense element. AG/AARP note that this result can be achieved by either setting the lead/lag values to zero or setting the test year income tax expense amount to zero within the CWC computations, and this “setting to zero” approach for income tax expenses was employed by ComEd in its formula rate case, Docket No. 11-0721. AG/AARP note that ComEd is also deferring all of its income tax liability due to bonus depreciation and other favorable tax deductions it is able to claim, and suggest that same result is necessary to determine AIC’s CWC allowance in this case.

AG/AARP recommend that the Commission reject AIC's argument that it has a long-standing practice of employing statutory tax rates and payment dates when calculating its income tax expense for revenue requirement purposes,” therefore AIC does not distinguish between current and deferred tax expense, nor does it include permanent tax differences in its income tax expense calculations. As noted by Mr. Brosch, there is no dispute regarding how to calculate incomes taxes, the use of statutory tax rates or the treatment of permanent tax differences in the ratemaking income tax expense calculation; however he states that AIC confuses the calculation of income tax expense with the CWC treatment of cash flows associated with income taxes. AG/AARP argue that CWC that is includable in rate base is focused on the timing of cash flows through the utility, rather than how to quantify income tax expense for ratemaking purposes.

AG/AARP state that the record evidence shows that in AIC’s case, no income taxes have been payable for several years and AIC is in a large federal income tax loss carry-forward position that insures that no taxes will be payable through the end of 2013, due to AIC’s utilization of bonus depreciation and tax accounting changes. AG/AARP suggest that income taxes that are not payable to the government are “deferred” income taxes which are non-cash expenses properly excluded from lead lag studies of CWC. AG/AARP opine that Mr. Brosch’s proposed adjustment simply recognizes that unless utility income taxes are currently payable in cash to the governments, there can be no CWC needs associated with such taxes.

While AIC claims that including these tax amounts in the CWC calculation will maintain a consistent treatment of income tax expense for ratemaking purposes, AG/AARP believe this argument misses the point of CWC. AG/AARP note that Mr. Brosch testified that it is always necessary to isolate and exclude non-cash expenses such as depreciation expense, amortization expense, and deferred income taxes when calculating CWC, and this is a routine practice that is widely accepted in Illinois and other states.

AG/AARP assert that AIC's application of revenue and expense lead/lag calculations of about $77 million in Income Taxes needlessly augments AIC's CWC request, and this approach should be rejected in favor of removing these amounts from the CWC lead/lag calculations. AG/AARP state that the operating expense input amounts in column (b) of AG/AARP Ex. 3.1 at 2 should be updated in the Commission's ordered amounts in this docket, and then applied to the CWC factor amounts shown in column (k) to derive total CWC to be included in the AIC formula rate base. While AG/AARP expect the result of such updating to be negative CWC, this result is indicative of the fact that AIC's ratepayers, employees, vendors, and taxing authorities, rather than its investors, are supplying the net CWC that is required to operate the business.

iv. CUB Position

CUB argues that zero revenue lag and expense lead values should be assigned to AIC's income tax expense because 2010 adjusted income taxes are substantially negative, and this approach is consistent with the approach used in Docket No. 11-0721, where ComEd was also deferring all of its income tax liability due to bonus depreciation and other favorable tax deductions it was able to claim. CUB suggests AIC is in the same position here, noting that for 2010 more than 100% of its income taxes are "deferred" taxes. While AIC opines that it does not distinguish between current and deferred tax expense, CUB avers that whatever AIC's practice may be, AIC should not collect CWC from ratepayers for taxes it did not actually pay. CUB recommends the Commission adopt the adjustment of AG/AARP to avoid a misstatement of AIC's true CWC needs.

v. Commission Conclusion

The Commission notes that on the issue of income tax lead and lag, AIC states that it utilized statutory income tax rates and payment dates when determining CWC. AIC believes that this is consistent with Commission practice of not considering current and deferred income taxes separately when calculating CWC. AIC notes that AG/AARP suggest setting the revenue lag and expense lead days be set at zero for income taxes because AIC's current income taxes are substantially negative, and more than 100% of AIC's 2010 income taxes are actually non-cash deferred income taxes. AIC believes AG/AARP's method is not only inconsistent with Commission practice, but it disrupts the balance between the ratemaking cost of service and the inputs to the CWC calculation. The Commission notes that Staff recommends the Commission adopt AIC's position on this issue, as it is consistent with past Commission practice.

AG/AARP, however, recommend that the Commission set the revenue lag days and the expense lead days at zero, since AIC's adjusted income taxes currently payable are negative. AG/AARP contend that since more than 100% of AIC's test year income taxes are actually non-cash deferred income taxes, there is no current period cash flow that could contribute to CWC. AG/AARP note that the approach it recommends was the method adopted by the Commission in Docket No. 11-0721. CUB also recommends that the Commission set the revenue lag and expense lead values to zero due to AIC's 2010 adjusted income taxes being substantially negative, asserting that this is consistent with Docket No. 11-0721.

In response, AIC argues that in contrast to ComEd, AIC calculates income tax expenses based on statutory rates, while ComEd calculates its income tax expense based on actual rates. AIC asserts that as the two methodologies are not aligned, it would be inappropriate to impose the method in the ComEd docket on AIC.

The Commission finds that AIC, as supported by Staff, has proposed the appropriate method in this docket for determining the appropriate income tax lead and lag. The Commission agrees that it has a long-standing practice of not considering current and deferred income taxes separately. The Commission finds no evidence present in this docket to cause it to vary from this treatment. The Commission recognizes that a different result was adopted in the ComEd docket, Docket No. 11-071; however, the Commission recognizes that ComEd and AIC calculate income taxes using different methodologies. Should those methodologies align in the future, or new evidence be presented, the Commission will certainly re-visit this issue in future proceedings.

d. Vacation Pay

i. AIC Position

AIC notes that Staff, AG/AARP, and CUB propose to deduct from rate base the accumulated liability for vacation pay on AIC’s balance sheet as of December 31, 2010. AIC contests this adjustment as improper ratemaking because the liability balance is not a source of non-investor supplied funds. In their direct testimony, CUB and AG/AARP justified their deduction in part because AIC’s CWC study did not reflect the longer lag in payment for vacation pay. AIC agreed on rebuttal to modify its calculation of payroll expense lead days to reflect the longer lag between the accrual and payment of vacation expense. AIC believes this is the proper ratemaking for vacation pay.

AIC states that CUB and AG/AARP balked at AIC’s adjustment to CWC as insufficient because it did not reflect the full impact of the vacation accrual; however, AIC argues it is improper to adjust payroll and withholding expense lead calculation to reflect anything other than the incremental variation in the annual accrual. AIC suggests the incremental variation in accrued expense is the only change reflected in the income statement, and thus it should be the only change that is reflected in AIC’s CWC when looking at the timing of cash receipts and cash operating statements for 2010.

AIC recommends the Commission adopt AIC's adjustment to CWC, as proposed on rebuttal, to reflect the longer lag between accrual and payment of vacation expense, and reject Staff, AG/AARP, and CUB's rate base deduction. AIC suggests that since the incremental variation in the annual accrued expense is the change reflected in AIC's income statement, the modification to the calculation of payroll expense leads should reflect that incremental change, and no further rate base adjustment to deduct the accrued liability is warranted.

ii. Staff Position

Staff recommends the Commission accept the proposal made by AIC witness Heintz to increase lead days for payroll in order to reflect the effect of accrued vacation days on CWC. Staff states that it has incorporated Mr. Heintz's proposal in its CWC calculation, and notes that AIC's proposal includes the year-over-year change in the level of the vacation accrual between the test year and the prior year. Staff asserts, however, that AIC's proposal does not include the balance of accrued vacation. Staff suggests it addresses the proper treatment of the balance of vacation pay accrual as an operating reserve in rate base.

iii. AG/AARP Position

AG/AARP suggest that the liability for vacation pay represents the total vacation pay accrued in excess of what has actually been paid. AG/AARP note that the vacation pay is, in effect, disbursed in the year following the year in which the liability for earned vacation is accrued, as the employees use their vacation time. This lag in payment for vacation pay is well in excess of the lag in payment of regular employee salaries and wages, and that actual lag in payment for vacation pay should be recognized in the determination of rate base.

AG/AARP state that in AIC's Initial Brief, it explained that AIC's calculation of CWC did not properly account for the payment lag associated with accrued vacation pay, in that it did not distinguish its treatment of regular payroll expense from that of accrued vacation pay expense. AG/AARP suggest the former has a lag of only 11.39 days, whereas the lag for the latter can be as much as one year. Therefore, AIC's rate base should be modified to reflect the lag by treating accrued liability for vacation pay as an operating reserve and deducting it from rate base.

iv. CUB Position

In response to the recommendations proposed by CUB and AG/AARP to deduct accrued vacation from rate base, CUB notes that AIC proposed to instead reflect the vacation accrual in its lead-lag study. CUB suggests that this is not the most appropriate way to reflect accrued vacation.

CUB's position is that the most appropriate method of adjusting AIC's rate base to account for accrued vacation liability is to treat the balance as a direct offset to rate base. If an adjustment was instead made to AIC’s lead-lag study, CUB suggests that a very long lag in payment must be reflected. Instead, CUB notes AIC adjusted the payroll expense lead, increasing it from 11.39 days to 13.12 days, based on the year-over-year change in the vacation accrual between the test year and the prior year, and applied an expense lead of 365 days. CUB argues this does not comply with the only other formula rate plan decision made to date, Docket No. 11-0721.

v. Commission Conclusion

AIC indicates it agreed, in response to criticism by other parties, to modify its calculation of payroll expense lead days to reflect the longer lag between the accrual and payment of vacation expense. AIC believes this is the proper ratemaking for vacation pay. AIC states that CUB and AG/AARP complain that AIC’s adjustment to CWC is insufficient because it did not reflect the full impact of the vacation accrual. AIC argues that it is improper to adjust payroll and the withholding expense lead calculation to reflect anything other than the incremental variation in the annual accrual. AIC suggests the incremental variation in accrued expense is the only change reflected in the income statement, and thus it should be the only change that is reflected in AIC’s CWC when looking at the timing of cash receipts and cash operating statements for 2010.

Staff recommends the Commission accept the proposal of AIC to increase lead days for payroll in order to reflect the effect of accrued vacation days on CWC. Staff states that it has incorporated this proposal in its CWC calculation, and notes that AIC's proposal includes the year-over-year change in the level of the vacation accrual between the test year and the prior year. Staff asserts, however, that AIC's proposal does not include the balance of accrued vacation, which Staff addresses as an operating reserve in rate base.

The Commission notes that AG/AARP also argue that AIC's rate base should be modified to reflect the lag by treating accrued liability for vacation pay as an operating reserve and deducting it from rate base. CUB notes that in response to the recommendations of AG/AARP and CUB, AIC now proposes to instead reflect the vacation accrual in its lead-lag study. CUB complains that this is not the most appropriate way to reflect accrued vacation, and CUB submits that the most appropriate method of adjusting AIC’s rate base to account for accrued vacation liability is to treat the balance as a direct offset to rate base. CUB argues that AIC's adjustment of the payroll expense lead based on the year-over-year change in vacation accrual does not comply with the Commission's finding in Docket No. 11-0721.

The Commission agrees with AIC and Staff that it is appropriate to increase the lead days for payroll in order to reflect the effect of accrued vacation days on CWC. The Commission recognizes that the parties have included in this section the arguments on an accrual to rate base due to vacation pay, and the Commission will address those arguments later in this Order.

2. ADIT – FIN 48

Generally ADIT quantifies the income taxes that are deferred when the tax law provides for deductions with respect to an item in a year other than the year in which the item is treated as an expense for financial reporting purposes. For regulated entities, ADIT is treated as a no-cost source of capital that reduces rate base.

a. AIC Position

AIC notes that the Financial Accounting Standards Board ("FASB"), Financial Interpretation 48 ("FIN 48") issue concerns the appropriate ratemaking treatment of so-called "FIN 48 liabilities," which AIC states is a relatively new issue before the Commission. AIC notes this issue was first raised in AIC's last rate case, Docket No. 11-0279/11-0282, however, the electric portion of that docket was dismissed upon the filing of the petition initiating this proceeding. AIC states this issue re-surfaced in the pending Illinois-American Water Company rate case, Docket No. 11-0767, although the Commission has not yet entered a final order in that docket. As far as AIC is aware, FIN 48 was not an issue in the ComEd formula rate proceeding, Docket No. 11-0721.

AIC opines that FIN 48 instructs public companies how to analyze, quantify, and account for the consequences of tax positions that may be disputed by tax authorities. AIC summarizes FIN 48 as the amount of tax that AIC and its outside auditors have concluded it is "more likely than not" will eventually be paid to taxing authorities in connection with the uncertain position must be reflected on the balance sheet as a tax liability, and interest and penalties must also be accrued.

AIC notes that Staff and certain intervenors believe that AIC's FIN 48 liabilities of approximately $40 million are of the same character as ADIT and should be deducted from rate base for the same reason ADIT is deducted from rate base: because ADIT represents a source of cost-free capital to the utility. As AIC witness Warren testified, however, deducting FIN 48 balances from rate base would encourage utilities to not take aggressive tax positions; tax positions that AIC believes all parties agree are beneficial to ratepayers.

AIC notes that FIN 48 liabilities share similar characteristics with conventional ADIT liabilities in the sense that both can be considered a "loan" from the government. In both cases, AIC suggests the term of this "loan" is the period between when taxes are due and when they are actually paid. AIC notes that a utility may claim accelerated tax depreciation for an asset on its return and, by doing so, reduce its current-year tax liability. Accelerating tax deductions does not change the overall tax expense of the utility; it only defers the payment of taxes. AIC avers that the deferral of taxes is like a "loan" that will be repaid in future years as available tax depreciation has been claimed.

AIC posits a situation where instead of claiming accelerated tax depreciation over a number of years, a utility decides to deduct the entire cost of an asset in one year. AIC notes that doing this would result in a larger tax deduction, for the simple fact that expensing 100% of an investment in one year will result in less taxable income than deducting 20% of the same asset over five years, and argues that foregoing an opportunity to write-off 100% of an asset in one year would probably not sit well with the Commission.

AIC next suggests a situation where the utility decides to deduct 100% of the cost of an asset or investment, but after filing its return learns that the Internal Revenue Service ("IRS") is challenging taxpayers who took the same or similar deduction. AIC states that the utility then engages tax experts and accountants who advise that it is “more likely than not” that the IRS will disallow the previously taken deduction. Using the two examples above, AIC states the consequence to the utility is that it will have to pay an amount of tax as if it had deducted only 20% of the asset instead of 100%, while interest and penalties will also be assessed from the date the return was filed until the additional taxes are paid – and the utility will not know when the tax must be paid until the IRS completes its review. In the meantime, AIC notes the utility records the difference between the taxes paid and the additional tax and penalties the IRS “more likely than not” will eventually demand as a FIN 48 liability.

Staff and Intervenors argue that because the utility has access to FIN 48 amounts until those amounts are paid, these “non-investor supplied funds” should be treated as ADIT and deducted from rate base. AIC suggests there are several problems with this theory. AIC argues that regardless of what one considers to be the “source” of FIN 48 amounts, these amounts, unlike ADIT, are not available to the utility to invest in rate base. AIC states the book/tax timing difference represented by ADIT reverses over time on a predictable schedule, and the utility knows how much non-investor supplied capital will be available to it and over what period of time. AIC asserts that FIN 48 amounts, however, could become payable at any time, as the timing of repayment is solely a function of action by the IRS.

AIC also notes that interest and penalties do not accrue on amounts that represent ADIT; therefore ADIT truly represents a “cost-free” source of capital; while FIN 48 amounts are not interest free; there is a cost associated with the use of these funds. AIC also notes that no party advocating a rate base adjustment for FIN 48 purposes to include this cost in the revenue requirement. AIC submits, however, that FIN 48 amounts are not interest free capital supplied by ratepayers, as the tax expense would be the same whether or not AIC took the uncertain tax positions ("UTP"). If it has to pay the tax assessments, AIC states it will be to the taxing authorities since the taxing authorities are the source of the funds being held. AIC contends that ratepayers have absolutely nothing to do with these funds, and the issue is entirely between it and the IRS.

AIC also argues that deducting FIN 48 balances from rate base unfairly punishes utilities that take aggressive tax positions that may benefit ratepayers. AIC suggests it is unreasonable in the first instance to disregard expert judgment that FIN 48 balances “more likely than not” will be repaid to the government, noting that if FIN 48 balances are paid to the government, these funds are not, by definition, “available” to the utility on a “cost-free” basis or otherwise. Conversely, AIC states that if the utility does prevail and the deductions are allowed, the FIN 48 balances will be re-characterized as ADIT and deducted from rate base in a future proceeding.

AIC claims that other jurisdictions have recognized the importance of maintaining the incentive for utilities to take UTPs, and urge the Commission to join those other jurisdictions’ treatment of FIN 48. AIC notes that CUB witness Smith recently wrote a paper on FIN 48 in which he acknowledges that, ideally, the interests of the utility and its customers should be aligned, and since there is an economic cash flow benefit of accelerating tax deductions, the rate process should encourage the utility to make tax decisions that are prudent economically.

AIC states that state commissions have echoed Mr. Smith’s sentiment in their ratemaking treatment of FIN 48 liabilities, indicating that Missouri, Kentucky, and Washington appear to have adopted AIC's position. AIC states that in Application of Kentucky-American Water Company for an Adjustment of Rates, Case No. 2010-00036, the Kentucky Attorney General argued the utility’s FIN 48 liabilities represented a source of zero-cost capital that should be treated as ADIT and passed through to ratepayers. (Order, Case No. 2010-00036, 2010 Ky. PUC LEXIS 1479, **29-30 (Ky. Pub. Serv. Comm’n Dec. 14, 2010)) AIC states that the Kentucky Commission, citing Missouri and Washington decisions, rejected the Kentucky Attorney General's argument and held that “[i]f the IRS ultimately allows the deduction ... ratepayers and shareholders will benefit from the tax deferral. If the IRS disallows Kentucky-American’s deduction, Kentucky-American has stated it will not seek recovery for interest and penalties imposed by the IRS and the ratepayers will not be negatively affected.” (*Id.* at 20)

AIC suggests there is no equitable principle that justifies providing a benefit to ratepayers for the temporary use of funds that did not come from ratepayers, and which are likely to be repaid with penalties and interest. When AIC pays these funds to the government, as it more likely than not will, under the Staff and Intervenor approach, ratepayers will get to keep the rate base deduction, until the next rate case, but AIC will not get to keep the underlying funds. AIC argues that this is an untenable result, and it should be rejected.

b. Staff Position

Staff recommends the Commission accept the AG/AARP adjustment to ADIT for amounts that have been identified by AIC’s tax experts as UTPs, since these amounts represent cost-free capital at the present time. Staff notes AIC summarizes the disagreement with AG/AARP as the proper treatment of this capital in the ratemaking process after it is procured, but before it is paid back. Staff states that AIC agrees with the following points on the issue of such capital:

1. AIC has in its possession a quantity of capital which it procured by means of filing income tax returns;

2. The capital at issue here resulted from claiming tax deductions which experts have concluded AIC is more likely than not going to lose;
3. When AIC loses the deductions, it will pay the capital back to the taxing authorities with interest.

Staff states the uncertainty of point number 3 is the crux of the issue. While it is not at all certain that AIC will lose deductions, there is no question that during the period of when the loss of those deductions is uncertain, AIC holds a quantity of funds for which there is no present cost.

Staff notes that AIC agrees that the FIN 48 amounts are not supplied by shareholders. Further, Staff argues that cost deductions on any tax return represent a level of uncertainty with regard to the final IRS determination of taxable income, while AIC admits that no IRS tax assessment exists for the amounts at issue in the revenue requirement. Staff asserts that under AIC's proposal, if the IRS allows the tax deduction associated with the FIN 48 reserve, customers would not receive the benefit of the deferred tax credits until the first rate case after the IRS completes its review of the issues that gave rise to the FIN 48 reserve. Further, Staff suggests these determinations can take a long time to occur, and may result in a settlement amount that is materially smaller than the original amount AIC recorded. Staff opines that AIC has proposed no mechanism to protect customers from the increased rates they did not deserve while awaiting the IRS to complete its review of the issues that gave rise to the FIN 48 reserve.

Staff notes that AIC dismisses Mr. Smith's testimony concerning FERC guidance with respect to FIN 48, arguing that because it states that it is for financial and reporting purposes only, and does not prejudice ratemaking practice or treatment, that the guidance is not relevant to this proceeding. Nonetheless, in Staff's opinion, the Commission should consider the FERC guidance. Staff notes that because this case uses a formula based upon the FERC Form 1 costs, the FERC guidance is especially relevant. Staff notes that FERC sets forth guidance that certain classifications that are required or permitted under FIN 48 are not permitted under FERC reporting, stating that:

> This is an important measurement objective of the Commission's Uniform Systems of Account because accumulated deferred income tax balances, which are significant in amount for most Commission jurisdictional entities, reduce the base on which cost-based, rate-regulated entities are permitted to earn a return. FIN 48, which does not permit a liability for uncertain tax positions related to temporary differences to be classified as a deferred tax liability, frustrates this important measurement objective. Therefore, entities should continue to recognize deferred income taxes for Commission accounting and reporting purposes based on the difference between positions taken in tax returns filed or expected to be filed and amounts reported in the financial statements.

However, Staff states the language in the FERC guidance that AIC uses to support its position is as follows:

> This guidance is for Commission financial accounting and reporting purposes only and is without prejudice to the ratemaking practice or treatment that should be afforded the items addressed herein.

Staff argues that this sentence expressly states that the purpose of the FERC guidance is for the reporting of financial information in the FERC Form 1, which provides the inputs for the formula rates. Staff suggests this sentence indicates that FERC cannot preempt companies' rights to present evidence in a ratemaking proceeding regarding the appropriate treatment of the FIN 48 amounts; it does not indicate that the FERC guidance on this issue should be ignored. In this docket, Staff opines that the evidence presented by AIC is insufficient to dismiss the FERC guidance on the proper inclusion of FIN 48 amounts in the ADIT balance that reduces rate base as reported in AIC's FERC Form 1 and to require ratepayers to pay a return on capital for which AIC has yet to incur a cost.

c. IIEC Position

Under FIN 48, IIEC notes that AIC is required to record a liability on its books for any tax deferral claimed on its tax returns that is more likely than not to be rejected by the taxing authority and require payment of an amount of deferred taxes. IIEC states that an expert assessment of the likelihood that a tax position will be rejected is required to determine the proper treatment of a tax position under FIN 48, and that claimed deductions based on UTPs must be recorded as offsets to AIC's balance of ADIT. Because ADIT is a negative component of rate base, IIEC avers that recognizing UTPs as an offset to ADIT has the effect of increasing the rate base AIC proposes to use to set its rates. While AIC witness Stafford reports that AIC's UTP reduction to ADIT is approximately $43.7 million, IIEC argues that AIC's proposed $43.7 million offset to its deferred income taxes would overstate the rate base appropriately used for ratemaking.

IIEC notes that in prior years, AIC has taken tax deductions that reduced its state and federal income taxes, but that were not reflected in the income tax expense AIC included in its delivery service rates, with the resulting reduction in the taxes AIC paid reflected in its ADIT balance. As a result, IIEC states that AIC is currently realizing the full benefit of these tax deductions, and it is appropriate that the deferral of taxes the utility is enjoying be recognized (through the associated ADIT) in a reduction to the rate base used to set rates. IIEC opines that the effect of a tax deferral is an interest free loan of non-shareholder capital; however the current treatment of UTP deferrals does not recognize the amount of that loan as interest free capital on which AIC is not entitled to earn a return. IIEC states that AIC's proposed recognition of UTPs reduces ADIT, increases rate base, and negates recognition of the interest free capital supplied by ratepayers through rates that include AIC's unreduced tax expense. IIEC suggests that under these circumstances, UTPs should not be an offset to ADIT.

IIEC asserts that the issue in this case is not the appropriate accounting for UTPs or AIC's identification of its UTPs, but rather, how should the risks of AIC's tax positions be apportioned between AIC and its ratepayers? IIEC notes that AIC acknowledges that this is an issue of ratemaking policy, and its expert Mr. Warren advocates the adoption of a ratemaking treatment that encourages AIC to take aggressive tax positions, with AIC also claiming that its position is supported by considerations of fairness. IIEC suggests however, that AIC and its ratepayers have divergent views of fairness in these circumstances. At an unknown future date, with a final determination by the IRS, a change in AIC's assessment of the uncertainty, or other events, each of AIC's UTPs will be resolved. IIEC opines that the Commission's ratemaking treatment of UTPs should be guided by the effects of the UTP claim before and after that resolution.

IIEC notes that AIC claims that fairness requires more than permitting AIC to recover the interest on uncertain deferred tax amounts it must accrue under FIN 48 pending resolution of the UTP. AIC also claims it must be protected against any loss of the return it would have earned if it had not taken the uncertain tax deductions. In fact, IIEC states that AIC wishes to be in the same position it would have occupied had it not taken the uncertain tax position which is the subject of the UTP. IIEC claims that AIC's position is that (a) the Commission should, encourage aggressive tax positions, because they may pay off with a win, even though AIC's experts have determined that a win is unlikely, (b) any costs arising while the UTP remains unresolved should be paid by ratepayers, and (c) regardless of the resolution of the UTP, AIC must be 100% protected against any financial consequences.

IIEC suggests that fairness from the ratepayers' perspective looks different, noting that AIC has the responsibility for prudent management of its business, and it is compensated for the risks of that responsibility with a statutorily set rate of return. AIC's business responsibilities include both tax planning and defending its tax positions, and although AIC is the party best equipped and positioned to manage the risk represented by UTPs, IIEC argues that AIC's proposal exposes the utility to none of that risk. IIEC suggests that AIC is seeking to hold ratepayers responsible for all possible financial risks associated with its tax position, while the only way ratepayers can benefit under AIC's proposal is if the UTP is allowed. But, even in that circumstance, IIEC opines that AIC keeps the benefits of the unreduced rate base it enjoyed while a resolution was pending, and ratepayers fail to realize any benefit while the UTP is pending or after a favorable resolution, and this resolution is reflected in rates.

In IIEC's view, it is premature as a matter of policy to exclude these deferred taxes from ADIT until a final resolution is made. IIEC notes that under AIC's proposal, until it is determined that the deduction is not allowed and AIC is required to pay the associated taxes and interest, AIC continues to enjoy the benefit of an interest free loan. IIEC argues that over the same period and for some time afterwards, ratepayers carry the entirety of the risk and enjoy none of the reward.

IIEC states that one legal constraint that bears on this issue is the Act's requirement that the rate base used to set rates include only the value of investment used to provide regulated service (see Section 9-211 of the Act). IIEC argues the loan of ratepayer funds described above should not be included through a reduction to the ADIT balance offsetting rate base.

d. AG/AARP Position

AG/AARP note that the ADIT-FIN 48 balances represent the amount of deferred tax liabilities that have been reclassified to FIN 48 liabilities related to UTPs that may ultimately have to be paid to the government. AG/AARP state that AIC reduced the balance of ADIT deducted from its delivery services plant in service, which has the effect of increasing the rate base and AIC's revenue requirement, to reclassify certain ADIT related to UTPs. AG/AARP aver that AIC shows debit balances of ADIT designated as ADIT FIN 48 for both state and federal taxing jurisdictions, with the federal balance at $35,701,000, and the balance of ADIT FIN 48 – State at $7,994,000.

AG/AARP witness Effron takes issue with AIC's unsupported reduction of the ADIT balance and corresponding increase to its rate base, instead recommending that these non-investor supplied funds be restored to the balance of ADIT (which reduces rate base) based on his analysis of AIC information related to these deferred tax amounts. Based on responses to AG data requests, AG/AARP suggest that the FIN 48 liabilities as of December 31, 2010 represent liabilities associated with the 2005-2006, 2007-2009, and 2010 audit cycles, and relate to what AIC describes as UTPs on casualty loss deductions, mixed service costs, and deductions for T&D repairs.

AG/AARP argue that AIC's reduction of the ADIT to reflect the reclassification as FIN 48 liabilities is not justified and should be rejected by the Commission. As Mr. Effron explained, until these deferred tax liabilities are actually paid to the relevant taxing authorities, they represent non-investor supplied funds that are available to AIC, a fact that is not disputed by AIC. AG/AARP assert that it is now known that certain of the balances will not have to be paid, and the undisputed evidence shows that it is highly likely that much of the remainder of the FIN 48 liabilities will not have to be paid, and therefore should be treated as ADIT for the purpose of determining AIC's rate base.

Generally speaking, AG/AARP claim that any uncertainty associated with these FIN 48 tax deduction amounts may be removed by: (1) the review of the technical merits of the position by the relevant taxing authority and expert; (2) the expiration of the statute of limitations related to the tax deduction; or, (3) a law change or court decision. In response to AG Data Request 2.17, AIC stated that the 2005-2006 audit cycle settled in June 2011, and the actual payment related to this cycle was $3,212,000 (Schedule DJE-1.2), compared to a FIN 48 liability of $8,899,000 at 12/31/10 (both stated on a jurisdictional basis). Thus, AG/AARP state the remaining $5,687,000 of the FIN 48 liability related to the 2005-2006 audit cycle should be classified as ADIT and deducted from rate base.

Also, in response to AG DR 5.03, AIC indicated that the 2007 audit cycle was expected to settle in 2012 with a payment of $858,000 (Schedule DJE-1.2) on a FIN 48 liability of $1,392,000. The remaining $533,000 of the FIN 48 liability related to the 2007 audit cycle should also be classified as ADIT and deducted from rate base. AIC did not dispute Mr. Effron's testimony on the point that these amounts identified through discovery will, in fact, not have to be paid.

In addition to these certain determinations regarding these FIN 48 amounts, Mr. Effron testified that he believed it is highly likely that much of the remainder of the FIN 48 liabilities will not have to be paid for two reasons. First, AG/AARP note that AIC is accruing interest expense on only $8.4 million of the FIN 48 tax liability as of December 31, 2010. AG/AARP suggest that the main reason that this is so much less than the FIN 48 liability as of that date is the availability of net operating loss carry forwards ("NOLs"), meaning that even if the UTPs result in disallowances, the disallowances will not actually result in tax payments to the extent that there are NOLs available to offset those disallowances. AG/AARP argue that to the extent that these deferred tax assets can be used to offset FIN 48 income tax liabilities, there is a double counting of the NOLs and the FIN 48 deferred tax items, and it is improper to include both in rate base.

AG/AARP state that another reason that it appears that AIC is unlikely to have to pay these deferred tax items can be found in AIC's response to DR AG 2.20, in which AIC stated that it filed an application for a change of accounting method regarding the deduction and capitalization of expenditures under Internal Revenue Code ("IRC") Section 263 (a), and that it was currently working to calculate the effect of such modification but has not yet modified its accounting for repairs pursuant to Revenue Procedure 2011-43. In response to DR AG 5.02, AG/AARP note that AIC indicated that the tax position related to T&D repairs for 2010 will no longer be uncertain once the method change related to accounting for repairs pursuant to Revenue Procedure 2011-43 has been filed. Given that many other electric utility companies have already modified their accounting for repairs, with considerable tax savings, AG/AARP claim that it is quite likely that when AIC makes this modification to its tax accounting, the FIN 48 liability related to the T&D repairs deductions will be resolved without any further payment by AIC.

Based on the information supplied by AIC, AG/AARP assert that the remainder of the ADIT debit balances related to FIN 48 should be eliminated from the balance of ADIT deducted from plant in service, noting that elimination of these debit balances, in effect, reverses the reclassification of the ADIT balances to FIN 48 liabilities for the purpose of determining AIC's electric rate base. AG/AARP state that the effect of eliminating the deferred tax debit balances related to FIN 48, other than those balances that have actually been paid or are likely to be paid, is to increase the balance of ADIT by $39,618,000 and to reduce the electric rate base by the same amount.

AG/AARP suggest there is no dispute that this balance represents non-investor supplied funds as long as the balance is outstanding, and to the extent that any of the FIN 48 liability has been paid, such repayment will be reflected in the determination of the actual 2012 rate base. However, to the extent that AIC still has a FIN 48 liability outstanding in 2012, AG/AARP opine that that balance should be included in the ADIT balance deducted from the actual rate base used in the reconciliation, as by definition such amounts will not have been paid. In this regard, AG/AARP claim that the rate base deduction for the FIN 48 liability poses no risk to AIC as long as the rate base originally used to establish rates in a given filing is ultimately trued up to the actual rate base.

Given Mr. Effron's conclusion that AIC will not pay any interest on the FIN 48 liability that he proposes be deducted from AIC's rate base, AG/AARP note that he does not propose that interest on the FIN 48 liability be included in AIC's revenue requirement. However, if AIC does incur interest expense in 2012 on the FIN 48 liability, then AG/AARP argue that such interest for 2012 should be included in AIC's 2012 operating expenses in the determination of its actual revenue requirement in the reconciliation.

AG/AARP note that AIC disputes this proposed adjustment for FIN 48, claiming that its FIN 48 amount is not ADIT capital, and should not be treated as such. AG/AARP opine that AIC's position is that its internal experts and external auditors have determined as of December 31, 2010 it is more likely than not that AIC will have to pay the federal and state governments the income taxes that have been deferred and identified as FIN 48 amounts. However, notwithstanding this view, AG/AARP aver that AIC witness Warren admitted during cross that since December 31, 2010, AIC now knows for certain that a significant portion of the amounts identified as FIN 48 ADITS by AIC will not have to be paid.

AG/AARP complain that AIC never identified who these so-called "internal experts and outside auditors" were, nor did AIC present them to testify. Mr. Warren testified that he was not one of the "internal experts or outside auditors" referenced in his testimony, and that he, in fact, performed no analysis of the likelihood that AIC will have to pay the amounts as taxes. AG/AARP note that Mr. Warren acknowledged during cross-examination that his recommendation to reduce AIC's recognized ADIT and leave the FIN 48 amounts in AIC's rate base for ratemaking purposes essentially asks the Commission to accept the opinions of these unnamed referenced internal experts and external auditors.

AG/AARP suggest the Commission should reject Mr. Warren's invitation to rely on hearsay claims about the likelihood of having to pay certain FIN 48 ADIT amounts, especially in light of the evidence presented by Mr. Effron that these amounts have either been declared by AIC to be not owed to the government or are highly unlikely to ever be paid. AG/AARP aver that AIC's position appears to be based on the odd theory that the FIN 48 should be added to rate base based on the opinions of the "internal experts or outside auditors" as of December 31, 2010 – no matter how erroneous those opinions proved to be.

AG/AARP note that AIC, in its Initial Brief, cited two decisions – one by the Missouri state commission and the other by the Kentucky state commission – which rejected deduction of FIN 48 balances from the relevant utility's rate base. AG/AARP contend that these arguments ignore the fact that most of the ADIT amounts in questions will never be paid back to the government. AG/AARP argue that AIC's reduction of the ADIT to reflect the reclassifications as FIN 48 liabilities is not justified and should be rejected by the Commission. AG/AARP states that the effect of eliminating the deferred tax debt balances related to FIN 48, other than those balances that have actually been paid or are likely to be paid, is to increase the balance of ADIT by $39,625,000 and to reduce the electric rate base by the same amount.

As noted by Mr. Effron, if the best information available is that these FIN 48 liabilities will not have to be paid, then the starting point for ratemaking purposes should treat the FIN 48 liabilities as ADIT, and they should be deducted from rate base given their undisputed status as non-investor-supplied funds.

e. CUB Position

CUB notes that AIC has included in rate base debit balances of ADIT FIN 48 – Federal of $35.701 million and ADIT FIN 48 – State of $7.994 million. Though AIC claimed deductions on its tax returns and thus avoided paying income taxes, CUB states that AIC nonetheless seeks to ignore this source of non-investor supplied capital for ratemaking purposes. CUB argues that AIC's proposal for the treatment of its FIN 48 amounts would allow it to benefit by taking UTPs, claiming deductions on its tax returns, and charging ratepayers for deferred income tax expense but failing to reflect the non-investor supplied source of capital represented by the tax benefits claimed on its tax returns. CUB states that a FIN 48 liability represents the difference between AIC's position taken on a tax return versus the identification of "uncertain" tax positions as required for financial statement reporting. CUB notes that differences in the interpretation of tax law exist, and FIN 48 prescribes procedures to quantify "uncertain" tax positions, for which the estimates are accumulated in a temporary reserve until the position is no longer uncertain. CUB notes that certainty can be achieved by either a review of the technical merits of the position by the relevant taxing authority, the expiration of the statute of limitations or a change in the law. CUB opines that AIC is attempting to increase rate base because there is an uncertainty with some of its tax positions, and AIC would prefer to ignore the non-investor supplied source of funding represented by the tax savings it has received, for ratemaking purposes, until the uncertainty perceived by its tax experts is resolved.

CUB notes that the financial accounting for UTPs would require a company with such positions to create a "reserve" relating to the uncertain amounts. CUB states that AIC witness Warren testified that experts have concluded it is more likely than not that AIC's deductions will be disallowed by the IRS. However, Mr. Warren was not among those experts who made the estimates of AIC's "uncertain" tax positions, nor was he involved at all in determining which if any of AIC's positions were uncertain. CUB complains that since none of the "experts" provided testimony in this proceeding, it appears that Mr. Warren's opinion is based solely on his understanding that the consensus within AIC is that the amounts at issue are more likely than not to be paid out, though he does not know if there is anyone outside of AIC who would disagree with that position. CUB avers, however, that information in the record concerning AIC's 2011 results shows that AIC had in fact substantially over-estimated the uncertain income tax positions in 2010, and significant reversals were recorded in 2011.

CUB states that AIC agrees that it is required to adhere to the FERC Uniform System of Accounts ("USOA") for Electric Utilities with respect to recording liability amounts related to UTPs. CUB opines that AIC's formula rate plan should be based on the use of accounting information that complies with the FERC USOA as reported on AIC's FERC Form 1, and suggest that attempting to artificially increase rate base by adding FIN 48 amounts to rate base represents a deviation from the FERC accounting guidance and is contrary to the use of FERC USOA accounting information. CUB argues that various other electric utilities, such as American Electric Power, are appropriately applying the FERC accounting guidance and using for ratemaking purposes the deferred tax balances provided for under the FERC USOA that reflect their filed tax returns without regard to any FIN 48 adjustments. CUB suggests that the FERC accounting guidelines, which are captured in CUB witness Mr. Smith's adjustment, reflect the most appropriate regulatory accounting and ratemaking treatment of these tax deductions and should be required for AIC in the current case as well.

Mr. Warren further argued that FIN 48 amounts are a in effect a government loan, in which case CUB suggests a solution could be to reflect FIN 48 amounts as a rate base deduction and provide a rate of interest on that. Though Mr. Warren called that solution "half a loaf" because that would supposedly put AIC in a less favorable position than they would have occupied had they not taken the position in the first place, CUB notes that he agreed that it is a solution. If AIC does indeed have to pay the taxes associated with its FIN 48 amounts, at most, it could have an associated interest cost of 4%, which is well below AIC's requested cost of capital. If AIC does not have to pay the taxes, CUB states the FIN 48 amounts have a zero cost, similar to all other ADIT.

CUB notes that AIC in its Initial Brief cites two other decisions in which the non-investor supplied capital in the form of tax savings was not reflected as a rate base deduction. CUB opines that the cases cited by AIC in support of its position are not formula rate cases where the utility will reconcile its rates every year. CUB also indicates that AIC's Initial Brief at page 24, footnote 4, cites a April 2, 2010 Washington state decision in a Puget Sound Energy, Inc. ("PSE") rate case, WUTC Dockets UE-090704 and UG-09075, which is misleading because subsequent decisions of the Washington Commission have reached the opposite findings. CUB suggests that AIC fails to state that the Washington Commission in that case found that the reason for not adopting the adjustment to fully reflect the ADIT impact in that case was that the utility's uncertain repairs deductions at issue there had occurred outside the test year being used. Moreover, CUB avers that the Washington Commission has, in subsequent rate cases involving not only PSE but also PacifiCorp, required that the utility deduct from rate base as ADIT the full amounts of tax deductions, including uncertain tax deductions for repairs.

CUB avers that AIC's own records show that the experts significantly over-estimated the "uncertain" income tax positions in 2010, and further show that AIC actually recorded a credit (rather than an expense) for FIN 48 interest due when those over-estimated amounts were reversed in 2011. CUB asserts this supports Mr. Smith's recommendation to treat FIN 48 similarly to other impacts from tax deductions, i.e., as an offset to utility rate base. CUB states that until AIC is instructed to do otherwise, they have the use of this at best zero-cost or at worst low cost (maximum 4% interest bearing) source of funds. CUB therefore recommends the Commission recognize this source of non-investor supplied capital and adopt Mr. Smith's adjustment to reduce AIC's requested rate base by $43.695 million.

f. Commission Conclusion

The Commission notes that Staff and certain intervenors believe that AIC's FIN 48 liabilities of approximately $40 million are of the same character as ADIT and should be deducted from rate base for the same reason ADIT is deducted from rate base: because ADIT represents a source of cost-free capital to the utility. AIC suggests that deducting FIN 48 balances from rate base would encourage utilities to not take aggressive tax positions, tax positions that AIC believes are beneficial to ratepayers. AIC also notes that interest and penalties do not accrue on amounts that represent ADIT; therefore ADIT truly represents a "cost-free" source of capital; while FIN 48 amounts are not interest free; there is a cost associated with the use of these funds. AIC also notes that no party advocating a rate base adjustment for FIN 48 proposes to include this cost in the revenue requirement. AIC submits, however, that FIN 48 amounts are not interest free capital supplied by ratepayers, as the tax expense would be the same whether or not AIC took the UTPs.

Staff recommends that the Commission accept the AG/AARP adjustment for ADIT-FIN 48, suggesting that these funds are indeed a cost-free source of capital for AIC. Staff notes that AIC has proposed no mechanism to protect customers in case AIC would not have to pay the disputed amount, or pay an amount smaller than was reserved. Staff suggests that the FERC guidance on this issue should be considered by the Commission, despite AIC's dismissal of that guidance. Staff argues the evidence indicates that the evidence presented is insufficient to dismiss the FERC guidance on the proper inclusion of FIN 48 amounts in the ADIT balance that reduces rate base as reported in AIC's FERC Form 1.

The Commission notes that IIEC, AG/AARP, and CUB all put forward essentially the same arguments as Staff, and all recommend that the FIN 48 balances be deducted from rate base, suggesting that this decision is in conformity with the FERC guidance on FIN 48. The Commission also recognizes that this issue does not appear to have been present in the ComEd smart grid docket, Docket No. 11-0721. The Commission agrees with Staff and Intervenors' position that the FIN 48 amount represents a source of cost-free capital that should be reflected as a rate base deduction. The Commission does not believe that AIC's position provides any mechanism to protect customers while awaiting an IRS review. The Commission notes that under AIC's position, if the IRS does not disallow the tax deduction associated with the FIN 48 reserve, customers would not receive the benefit of the deferred tax credits in the form of a rate base reduction until the first rate case after tax returns are no longer subject to IRS review and adjustment. The Commission will therefore adopt for this proceeding the proposal to reduce rate base to reflect the FIN 48 balances of $35,695,000 for the federal and $7,993,000 for the state, net of the total expected payments on FIN 48 of $4,070,000, for a net reduction of $39,618,000

3. ADIT – Projected Additions

a. AIC Position

In establishing initial formula rates, AIC notes that Section 16-108.5(c)(6) of the Act requires adjustments to the FERC Form 1 data to reflect "projected plant additions and correspondingly updated depreciation reserve and expense for the calendar year in which the tariff and data are filed." AIC contends that while no party disputes that the adjustments for projected plant additions, depreciation reserve, and depreciation expense are appropriate, Staff and Intervenors argue that in addition to adjusting projected plant and depreciation reserve and expense, the Act also requires an adjustment to rate base to reflect ADIT generated by 2011 and 2012 plant additions.

AIC avers that this is incorrect, and that Staff and Intervenors have read a required adjustment into the Act that is not there. AIC notes the Act requires adjustments to three specific FERC Form 1 rate inputs: (1) projected plant additions, (2) depreciation reserve, and (3) depreciation expense. AIC opines that the legislature was presumptively aware that these three rate inputs do not represent the totality of costs and investments that must be reflected in rates, and suggest that the legislature was specifically aware of prior controversy concerning whether rate base adjustments for future plant investment must include "offsetting" adjustments for ADIT associated with the investment, noting that Section 16-108.5(j), citing Commonwealth Edison Co. v. Ill. Commerce Comm'n, 405 Ill. App. 3d 389 (2d Dist. Sept. 30, 2010), appeal denied, 350 Ill. Dec. 350 (Mar. 30, 2011). AIC states that it is clear the legislature knew what ADIT is, and the legislature determined to not require an adjustment to ADIT in establishing formula rates. By requiring adjustments to three specific rate inputs, AIC argues that the legislature is presumed to have intentionally excluded adjustments to other non-enumerated rate inputs. See Northern Moraine Wastewater Reclamation Dist. v. Illinois Commerce Comm'n, 392 Ill. App. 3d 542, 565, 912 N.E.2d 204, 225 (2nd Dist. 2009) ("Under the principle of *inclusio unius est exclusio alterius*, the enumeration of one thing in a statute is construed as the exclusion of all others."); State v. Mikusch, 138 Ill. 2d 242, 250 (1990) ("It is established in statutory construction that the expression of certain exceptions in a statute will be construed as an exclusion of all others."); New Jersey v. Delaware, 552 U.S. 597, 634 (2008).

AIC suggests the second reason the proposed adjustment to ADIT is contrary to law is because the adjustment would have the effect of establishing initial rates, and reconciling these rates, with figures that do not represent “actual costs." AIC notes the objective of performance-based formula rates is to “specify the cost components that form the basis of the rate charged to customers with sufficient specificity to operate in a standardized manner and be updated annually with transparent information that reflects the utility's actual costs to be recovered during the applicable rate year,” quoting a portion of Section 16-108.5(c). AIC states that ADIT for 2011 and 2012 plant additions cannot be gleaned or derived from the 2010 FERC Form 1, and suggests that the Staff and Intervenor calculations, which range from approximately $108 to $173 million, can hardly be said to constitute “transparent information” reflecting “actual costs” that will flow through to rates in a “standardized manner.” Where the EIMA requires rates to be set and subsequently reconciled based on “actual costs,” Staff and Intervenors instead propose to establish rates based on speculation about what they think the balance of ADIT may be in the future.

AIC suggests the Act precludes this sort of guesswork, and argues the legislature determined that FERC Form 1 provides the most suitable source of “transparent information that reflects the utility’s actual costs.” For the various reasons discussed by Mr. Stafford, including the ADIT impact of existing plant additions on future years and uncertain status of bonus depreciation, AIC claims that ADIT arising from projected plant additions cannot be readily determined – a fact which AIC suggests is confirmed by the large variances in the Staff and Intervenor proposals.

AIC notes that Staff and Intervenors claim that ADIT for future investment must be deducted from rate base to prevent rate base from being “overstated." AIC recognizes that the court in the ComEd decision in 2010 more or less agreed with this theory, but AIC suggests the court’s opinion is of no import here. AIC opines that rates established in a “traditional” Article IX rate case are presumptively just, reasonable, and adequate until the Commission approves new rates in a subsequent proceeding, and if the utility over- or under-recovers during the rate-effective period, there is no allowance for a refund to customers or a true-up for the utility. Given the uncertainty about how long rates will be in effect, combined with the lack of any mechanism to deal with over- or under-recovery, AIC claims there is an emphasis in traditional ratemaking on trying to ensure that the test year revenue requirement reflects future investment and expense as accurately as possible.

However, AIC submits that formula ratemaking is different, as there is no “test year” under formula rates. Historical costs are not adjusted for “known and measurable” changes, nor are forecasts prepared to develop a revenue requirement for a future period. Indeed, under traditional ratemaking, AIC notes that “actual costs” incurred by a utility are relevant only insofar as the costs establish a starting point for developing a test year. Under the Act, however, AIC’s initial formula rates are to be calculated using “actual costs” as reflected in the 2010 FERC Form 1, adjusted for plant additions, depreciation reserve, and depreciation expense through 2012 (the “calendar year” in which AIC filed its formula rate plan). AIC submits there is an obvious reason that the

General Assembly included the adjustment for projected plant and depreciation reserve and expense: in a period of significant incremental capital expenditures, they intended to lessen the regulatory lag in the utilities recovering their capital expenditures so that they have the cash on hand to make the investments.

That AIC's formula rates will not reflect ADIT on projected plant does not mean that rate base will be "overstated," noting that by the time rates are in effect for each successive update proceeding, AIC will have actually incurred the capital costs for that projected year. AIC asserts that formula rates are to be established based on "actual costs" and reconciled annually with "actual costs." AIC's first reconciliation, to be filed by May 1 2013, "shall reconcile (i) the revenue requirement or requirements established by the rate order or orders in effect from time to time during such calendar year (weighted, as applicable) with (ii) the revenue requirement for that calendar year calculated pursuant to the performance-based formula rate using . . . actual costs for that year as reflected in the applicable FERC Form 1 . . . ." Accordingly, AIC argues that initial rates must reflect actual ADIT as reported in the 2010 FERC Form 1. When these rates are reconciled in 2013, the 2012 FERC Form 1 will report actual ADIT recognized in AIC's books for calendar year 2012. AIC notes that any over- or under-recovery produced by rates in effect during 2012 will show up as an adjustment to rates established in 2013 (and effective as of January 2014), and that establishing and reconciling rates based on actual costs ensures that customers will pay rates based on actual costs, no more and no less.

AIC posits that the Staff and intervenor adjustments are ultimately an exercise in speculation; speculation about what AIC's actual 2012 revenue requirement might be, as opposed to how the Act says the revenue requirement must be calculated. AIC claims that the Act recognizes that using actual historical data to set rates prospectively could lead to over- or under-recovery, and establishes an annual reconciliation mechanism to deal with this, therefore the Staff and intervenor proposals should be rejected.

b. Staff Position

Staff recommends the Commission accept the AG/AARP adjustment to the balance of ADIT to reflect the estimated ADIT that will be generated by 2011 and 2012 plant additions. Staff notes that AIC focuses on the 2011 and 2012 ADIT, which is increased significantly due to bonus depreciation; however, this position was rejected in the ComEd order:

> Because federal tax laws regarding 2011 allow businesses like ComEd, currently, to depreciate plant additions at 100%, ComEd has use of funds now that it would not have otherwise normally have had access to without borrowing or other forms of financing. In effect, ignoring this windfall to ComEd would be to allow ComEd an interest-free loan at the ratepayers' expense for several months. It also would artificially increase rates until the time when a final order in the 2011 reconciliation docket takes place.

> It cannot have been the intention of the General Assembly, when enacting Section 16-108.5, to allow this statute to artificially raise rates for several months. (Docket No. 11-0721, May 29, 2012 Order at 59)

Staff suggests the facts and law are no different in this case, and note that the Commission rejected ComEd's request for rehearing on this issue. Staff claims it would be unreasonable for the AIC formula rate, which is based upon the same statute as ComEd's, to contain a different conclusion on the same issue as ruled upon in Docket No. 11-0721.

c. IIEC Position

IIEC states that the Commission and the Illinois Appellate Court have held that the Act bars Commission approval of a rate base that exceeds the value of investment prudently incurred and actually used in providing service. (See Docket Nos. 09-0306 et al. (Cons.), November 4, 2010 Order on Rehearing at 49; and Ameren Illinois Company v. Ill. Commerce Comm'n, 967 N.E. 2d 298, 359 Ill. Dec. 568, (Ill. App. Ct. 4th Dist. Jan. 10, 2012)) IIEC suggests this requires that the Commission's rate base determination reflect the values for Plant, Depreciation Reserve, and ADIT at a consistent point in time. IIEC notes the Commission has recently applied this same concept, consistent treatment of rate base components, in a formula rate determination, Docket No. 11-0721. IIEC argues that AIC's proposal to ignore the effect of ADIT on its rate base does not yield, as Section 16-108.5 requires, a determination of AIC's actual costs that is consistent with Commission practice and with the governing law, but will instead produce rates that are unreasonable.

IIEC notes that AIC proposes to determine its formula rates using a rate base that includes projected plant additions and the build-up in accumulated depreciation in the year following the FERC Form 1 year, but not the contemporaneous build-up in ADIT, with AIC arguing that recognizing the effect of ADIT on its projected rate base and capital costs is (a) prohibited because ADIT is not specifically mentioned in (and is therefore inconsistent with) Section 16-108.5 and (b) unnecessary because the neglected effect of ADIT on rate base will be captured in the true-up calculation.

IIEC opines that AIC's interpretation and application of the formula rate statute would preclude the Commission's performance of its duty to determine the amount of AIC's prudently incurred, reasonable costs used to provide service -- and to use only those costs in setting its rates. IIEC and other parties propose that the rate base used to set rates also incorporate a projection of ADIT for the period of the AIC plant additions. IIEC states that ADIT, which is the third largest component of rate base, is an offset to plant additions and reduces the rate base used to set rates, while ignoring ADIT would significantly overstate AIC's actual cost of service and thereby produce unreasonable rates.

IIEC states that not updating ADIT is not "consistent with Commission practice and law," as the formula rate statute requires, noting that the Commission and reviewing courts have recognized that such rate determinations under Article IX require the Commission to take account of the contemporaneous build-up of offsets to plant additions such as accumulated depreciation and the "companion" adjustment ADIT, to accurately measure rate base so that Section 9-211 is not violated. (See Docket Nos. 09-0306 et al. (Cons.), November 4, 2010 Order on Rehearing at 49; Commonwealth Edison Co. v. Illinois Commerce Comm'n, 405 Ill. App. 3d 389 at 405 (2nd Dist. 2010); Ameren Illinois Co. V. Illinois Commerce Comm'n., 967 N.E. 2d 298, 359 Ill. Dec. 568 (Ill. App Ct. 4th Dist. 2012)). IIEC argues this "companion" adjustment is a legally required part of "Commission practice and law" per Section 16-108.5(c)(1); and that the Commission must consider this rate base component as well as accumulated depreciation for a lawful determination under Section 16-108.5(c)(1).

Consistently, IIEC notes the Commission ordered recognition of ADIT in determining the rate base for formula rates in the ComEd formula rate case. The ADIT rate base component, if not others in addition, must be recognized if rate base is to be accurately determined, and later reconciliation credits or charges minimized. IIEC states the Commission recently held in the Docket No. 11-0721: “The goal should be to have rates accurately reflect costs, and reconciliation is merely a tool to correct and adjust unavoidable imbalances.” (Docket No. 11-0721, May 29, 2012 Order at 167)

IIEC opines that Section 16-108.5 does not expressly bar the Commission's consideration of ADIT in its determination of AIC's rate base, while at the same time, the Commission is expressly charged with implementing that provision to achieve the objective of the formula rates process: rates that provide for the recovery of the utility's actual costs of delivery services that are prudently incurred and reasonable in amount consistent with Commission practice and law.

IIEC avers that there is no inherent conflict between the provisions of Section 16-108.5 and the requirements of Article IX, and that there is no express prohibition on the Commission's consideration of revenue requirement components not specifically mentioned in Section 16-108.5. IIEC opines that the Commission's required Article IX review of the components of AIC’s proposed capital costs must take account of both accumulated depreciation and ADIT.

IIEC suggests that AIC’s argument that the reconciliation process makes recognizing a major cost element unnecessary is essentially meaningless. IIEC notes that any deviations from AIC’s actual, prudently incurred, and reasonable costs of service will be resolved by the reconciliation. However, IIEC contends that the provisions of Article IX, repeatedly referenced in the formula rate statute, do not allow the Commission to approve a rate base or a rate that is not prudent, just, and reasonable.

IIEC avers that under Section 16-108.5, the required reconciliation is only of revenue requirements and rates; there is no reconciliation of the revenues collected from customers through initial formula rates and AIC’s actual costs. IIEC contends there is no assurance that customer over-payments will be remedied through the statutory reconciliation process if initial formula rates vary from the best possible cost projections for the rate year.

IIEC argues that AIC's perverse interpretation of the formula rate statute would severely undermine the required Article IX review of proposed costs, and would undermine the Commission's mandate to determine the amount of AIC's prudently incurred, reasonable costs used to provide service, and to allow only such costs in setting AIC's rates. IIEC urges that this interpretation be rejected.

d. AG/AARP Position

AG/AARP note that AIC included $405,523,000 of 2011 and 2012 projected plant additions in its delivery services rate base, while also recognizing an associated increase in the balance of accumulated depreciation of $304,728,000 for 2011 and 2012. AG/AARP state the net effect is to increase rate base by $100,795,000. AG/AARP contend that AIC has not recognized the growth in ADIT directly related to the 2011 and 2012 projected plant additions. Given the ratemaking dictates of Section 16-108.5 of the Act, AG/AARP argue that it is appropriate to include the effect of the ADIT generated by the 2011 and 2012 plant additions in the calculation of the delivery services rate base.

AG/AARP witness Effron explains that when AIC reconciles the revenue requirement for 2012 developed in this case to the actual 2012 revenue requirement in its 2013 filing, there is no question that the rate base used in the actual revenue requirement calculation will reflect the actual balances of ADIT in 2012. Therefore, Mr. Effron states the ADIT generated by the 2011 and 2012 plant additions will ultimately be included in the calculation of the 2012 delivery services rate base. Unlike the other rate base issues addressed in this testimony, Mr. Effron suggests this issue will eventually be resolved by the reconciliation, and there would be little purpose in proposing an adjustment to increase ADIT if the only effect would be to increase the difference between the rate base used in this filing (which for simplicity is referenced as the "test year rate base") and the actual 2012 rate base. However, in the circumstances of this case, Mr. Effron indicates it does not appear that recognition of the ADIT generated by the 2011 and 2012 plant additions will increase the difference between the test year rate base and the actual rate base.

AG/AARP note that in 2011, the existence of 100% bonus depreciation provides AIC with a tax deduction equal to the amount of additions to plant in service, and in 2012 the existence of 50% bonus depreciation provides AIC with a tax deduction equal to one-half of the amount of additions to plant in service. AG/AARP state that this will lead to growth in the balance of ADIT in 2011 and 2012 well in excess of the growth that would take place in the absence of the bonus depreciation.

In addition, AG/AARP opine that AIC has filed an application for a change of accounting method regarding the deduction and capitalization of expenditures under IRC Section 263(a). While AIC has not yet modified its accounting for repairs, AG/AARP suggest the tax benefits are likely to be substantial when it does. For example, in Docket No. 11-0721, AG/AARP note that ComEd estimated the tax deduction associated with the Section 481(a) ("catch-up") component of this tax accounting change would be approximately $600 million, with a concomitant increase to the balance of ADIT of approximately $240 million. In these circumstances, Mr. Effron testified that it is appropriate to recognize the ADIT on the bonus depreciation in 2011 and 2012 as an offset to the growth in net plant.

In accordance with these conclusions, Mr. Effron recommends that an adjustment increasing the balance of ADIT related to 2011 and 2012 plant additions by $107,990,000 be made, which would result in the balance of ADIT deducted from plant in service in the determination of the delivery services rate base to increase by that amount. In the circumstances of this case, Mr. Effron noted that this adjustment would tend to reduce, rather than increase, any discrepancy between the test year rate base in this case and the actual 2012 rate base.

AG/AARP note that AIC witness Stafford opposes this recommendation, arguing that it only estimates the change in ADIT due to 2011 and 2012 projected plant additions without considering other changes to ADIT that would result from depreciating existing plant or whether bonus depreciation should be applied to all projected additions. Mr. Stafford further claims that it also does not reflect potential changes to other rate base items in 2011 or 2012.

AG/AARP suggest that these arguments are not persuasive, and while it is true that other items of ADIT are continually changing, it would make little sense to attempt to capture the effect of all these changes when the revenue requirement calculated in this case is ultimately going to be trued up to the actual revenue requirement in 2012. AG/AARP opine that it is the magnitude of the ADIT on the 2011 and 2012 plant additions that sets it apart and makes this adjustment necessary in order to reflect the best information available in setting rates.

Mr. Effron quantified an adjustment to rate base of $107,990,000 for the ADIT related solely to the bonus depreciation on 2011 and 2012 plant additions, and contends that AIC witness Stafford does not dispute this quantification, nor does he cite any potential changes in any other items of ADIT or other rate base items that would result in a material offset to the magnitude of the ADIT on the 2011 and 2012 plant additions. AG/AARP state that Mr. Stafford also failed to identify any plant additions in 2011 or 2012 that do not qualify for bonus depreciation. AG/AARP submit that Mr. Effron's well-reasoned adjustment to AIC's delivery services rate base is appropriate here in order to ensure that the rate base is not improperly inflated and correctly reflects changes to ADIT that are identifiable and significant.

e. CUB Position

CUB states that while AIC proposes to include 2011 and 2012 projected plant additions in rates, AIC also chooses to ignore the related substantial amounts of ADIT resulting from the 2011 and 2012 bonus federal income tax depreciation. CUB witness Smith recommends including the ADIT on 2011 and 2012 plant additions, for the difference between book and tax depreciation. Because the tax law provides for the opportunity for 100 percent bonus tax depreciation on 2011 qualifying assets and 50 percent bonus tax depreciation on 2012 qualifying assets, CUB asserts that this is a significant omission that, if not adjusted, will overstate rate base in the first case setting AIC's formula rates. CUB argues that this overstatement should be recognized now in order to help minimize the amount of 2011 over-collection that would likely result if this large impact is ignored now and only reflected in the 2011 reconciliation case.

CUB notes that AIC complains that an adjustment to ADIT due to 2011 and 2012 plant additions would merely be an estimate, and would not reflect potential changes to other 2011 and 2012 rate base items. However, CUB opines that AIC has already provided actual 2011 year-end ADIT in a data request response, and AIC also calculated and reflected its actual balances of ADIT for 2012 in its concurrent reconciliation docket, ICC Docket No. 12-0293.

CUB notes the Commission has already addressed this issue in the ComEd formula rate plan case, ICC Docket No. 11-0721. In that case, CUB states the Commission concluded that ignoring the ADIT directly related to jurisdictional plant increases would be ignoring accounting principles and appellate precedent, and further acknowledged that ADIT is a source of revenue for a utility, giving the utility use of funds now that it would not have otherwise normally had access to without financing. CUB notes that in Docket No. 11-0721, the Commission stated:

> In effect, ignoring this windfall to ComEd would be to allow ComEd an interest-free loan at the ratepayers' expense for several months. It would artificially increase rates until the time when a final order in the 2011 reconciliation docket takes place. It cannot have been the intention of the General Assembly, when enacting Section 16-108.5, to allow this statute to artificially raise rates for several months. (Docket No. 11-0721, May 29, 2012 Order at 59)

CUB suggests that each of the arguments articulated in the ComEd Order are applicable to the instant case, and argues that the artificial inflation of rates that would result from AIC's proposal would be even more egregious in this case, as it includes ADIT on 2012 plant which will not be reconciled for more than a year. Therefore, CUB recommends that the Commission adopt its proposed adjustment of $111.672 million.

f. Commission Conclusion

The Commission notes that in establishing initial formula rates, Section 16-108.5(c)(6) of the Act requires adjustments to the FERC Form 1 data to reflect "projected plant additions and correspondingly updated depreciation reserve and expense for the calendar year in which the tariff and data are filed." AIC contends that while no party disputes that the adjustments for projected plant additions, depreciation reserve, and depreciation expense are appropriate, Staff and Intervenors argue that in addition to adjusting projected plant and depreciation reserve and expense, the Act also requires an adjustment to rate base to reflect ADIT generated by 2011 and 2012 plant additions. AIC contends that this is incorrect, and that the Act only requires adjustments to three specific Form1 inputs: projected plant additions, depreciation reserve, and depreciation expense.

Staff recommends that the Commission adjust the balance of ADIT to reflect the estimated ADIT that will be generated by 2011 and 2012 plant additions. Staff notes that AIC's position was rejected in Docket No. 11-0721, and suggest that the facts and the law are no different in this case. Staff claims that it would be unreasonable for the AIC formula rate, which is based upon the same statute as ComEd's, to contain a different conclusion on the same issue. IIEC likewise recommends updating ADIT for 2011 and 2012 plant additions, arguing that to ignore ADIT would significantly overstate AIC's actual cost of service and would produce unreasonable rates. AG/AARP and CUB similarly urge the Commission to follow the precedent set in Docket No. 11-0721, and to update ADIT to reflect 2011 and 2012 plant additions.

The Commission agrees with Staff and intervenors and finds that it would be appropriate to incorporate in this Order a portion of the relevant conclusion from the Order in Docket No. 11-0721:

> . . . However, the statute is silent altogether with regard to ADIT and with regard to many other items that all agree must be included in, or deducted from, rates. If the Commission were to ignore ADIT on ComEd's plant investments, we would be ignoring basic accounting principles and appellate precedent. (See *Ameren Illinois Co. v. Ill. Commerce Comm.,* 2012 IL. App. (4th) 100962 at 31, 2012 Ill. App. LEXIS 175 (4th Dist. 2012), determining, with regarding to an ADIT adjustment to Ameren's rate base, that Section 9-211 of the Public Utilities Act requires that rate base cannot exceed the investment value that a utility actually uses to provide utility services.).
>
> ADIT, a derivative adjustment that is caused primarily by plant additions, is a source of revenue for a utility. Because federal tax laws regarding 2011 allow businesses like ComEd, currently, to depreciate plant additions at 100%, ComEd has use of funds now that it would not have otherwise normally have had access to without borrowing or other forms of financing. In effect, ignoring this windfall to ComEd would be to allow ComEd an interest-free loan at the ratepayers' expense for several months. It also would artificially increase rates until the time when a final order in the 2011 reconciliation docket takes place. It cannot have been the intention of the General Assembly, when enacting Section 16-108.5, to allow this statute to artificially raise rates for several months. In fact, this statute provides that the performance-based formula rate shall:

> Reflect the utility's actual capital structure for the applicable year, excluding goodwill, subject to a determination of prudence and reasonableness consistent with Commission practice and law.

(220 ILCS5/16-108.5(c)(2))

(Docket No. 11-0721, May 29, 2012 Order at 59-60)

As the Commission found in Docket No. 11-0721, it is appropriate under the facts presented in this docket to update the ADIT balances as requested by Staff and the Intervenors. The Commission finds that the adjustment quantified by AG/AARP, $107,990,000, which amount it appears AIC did not contest as incorrect, is the appropriate adjustment to be adopted on this issue.

4. Accrued Vacation Pay as Operating Reserve

a. AIC Position

AIC states that vacation pay is an accrued expense recorded on its balance sheet, which accrual represents the liability existing on AIC's books associated with vacation time earned by employees. Like other accrued expenses, AIC notes that the expense is recorded for employee services before compensation is paid, and as a result, there is a lag between the time vacation pay is accrued and the time the expense is paid.

AIC indicates that each January, an initial accrual is recorded to Account 920 to recognize the labor expense AIC will incur for the vacation pay employees will earn that year, and as employees take earned vacation that following year, the accrual is amortized off with monthly offsetting entries to Account 242. For AIC, the lag between the accrual and payment for the accrued compensated absences is approximately one year. AIC states the portion of the accrual reflected in the income statement is the decrease or increase at year-end to the accumulated liability, while the incremental change in the accrual is reflected in the CWC calculation as a reduction to that calculation through the payroll expense lead. Assuming a constant or expanding work force, AIC notes the accrual should increase slightly each year, as wages and salaries increase.

AIC notes that Staff, AG/AARP, and CUB all seek to deduct the amount of the accrued vacation pay at year-end 2010 from rate base. AIC contends that those parties cite two rationales for their rate base deduction: (1) AIC failed to account for the longer vacation pay lag in its CWC and thus the accrued liability represents a source of non-investor funds; (2) AIC included deferred tax debit balances in rate base to reflect the book-tax timing difference for vacation pay and thus the proper match would be to also include the related accrual. AIC contends that neither rationale is valid, and submits that it properly reflected the vacation pay lag in its CWC calculation. AIC submits that it properly included the ADIT balance in rate base without making a deduction for the accumulated liability balance, and notes that it compensated employees for vacation earned in 2010 before it filed this formula rate petition and before it collects 2010 payroll expense in rates.

AIC avers that both AG/AARP and CUB claim the accrued liability balance should be deducted from rate base because the longer lag in payment of the expense was not recognized in the calculation of CWC. AIC agreed and on rebuttal modified the calculation of payroll expense lead days to reflect the longer lag between the accrual and payment of vacation expense. Since the accrual on AIC's balance is adjusted to reflect the change in total liability, AIC states the only portion of the accrued expense that would ever be included in the income statement would be the annual increase or decrease to the overall accrual. Similarly, since the CWC analysis is intended to measure the timing of cash receipts and cash operating statements, AIC adjusted its CWC calculation by adjusting the payroll and withholding expense lead calculation to include the vacation accrual variation for the twelve months ending December 31, 2010.

AIC complains that in rebuttal testimony, AG/AARP and CUB reversed course and rejected an adjustment to CWC as an appropriate treatment to recognize the lag between accrual and payment. AIC's adjustment to CWC, AG/AARP and CUB claimed, was insufficient because it did not reflect the full impact of the vacation accrual, and AIC notes neither party offered a different adjustment to CWC on rebuttal. Instead, AG/AARP, CUB, and Staff (for the first time on rebuttal) argued the only proper treatment was a rate base deduction, claiming the accumulated liability is a source of funds for the utility. However, AIC suggests that premise is fundamentally flawed.

Because accrued vacation is due and payable within one year, AIC argues that its customers have not financed any of the 2010 expense prior to the Commission's issuance of an order in this proceeding and the collection in rates of 2010 payroll expense. Thus, AIC submits it will always be behind on cash collections for this expense item, and any incremental increase in that expense item, as AIC's payroll expense increases in future years during its EIMA investments, as more jobs are created and wages and salaries go up. Accordingly, there is no source of cash from 2010 accrued vacation expense that AIC already has on hand to fund rate base investments. AIC therefore argues that a rate base deduction of the accrued liability balance withholds revenue for an expense that AIC has paid out but, because of the deduction, will now never receive.

AIC notes that Staff agrees that for a liability balance to represent a source of non-investor supplied capital, the utility should receive the capital through rates before it has paid the expense, and that Staff agrees there is no evidence that vacation accrued in 2010 was not paid within a year. AIC contends Staff agrees any vacation accrued in 2010 would have been paid in 2011 before this formula rate petition was filed and before rates for this proceeding are in effect – so that by the time AIC has received any revenue from ratepayers for 2010 payroll expense, that accrued expense would have paid. As Staff also agrees that there is a lag between the time AIC pays the vacation pay, and the time that AIC receives the accrued expense in rates for that particular year 2010, AIC submits there is not and cannot be a free source of ratepayer funds to finance rate base related specifically to 2010 accrued expense.

Staff suggests the accrual still represents non-investor supplied funds because it is ongoing, and AIC agrees that each year an accrual is made for the vacation pay earned prior to AIC employees taking earned vacation days. However, the same is true for all of AIC's payroll expenses, in the sense that AIC continues to incur the expense every year. AIC notes that its cash disbursements for vacation pay are also ongoing, and there is not a year that passes where employees are not taking compensated days. More importantly, in the formula rate process, vacation pay that accrues in 2011 and 2012 will still be paid out by AIC before rates collecting that payroll expense even go into effect. AIC contends that since accrued vacation expense is due and payable within a year, it can never provide a free source of ratepayer funds to finance rate base.

AIC suggests that the crux of the parties' adjustment to deduct the accrued liability for vacation pay from rate base, and the crux of the Commission's rate base deduction in ComEd's formula rate proceeding, is the premise that the accrual represents a "source of non-investor supplied capital." However, as AIC has noted, this premise is false. AIC has explained that AIC accrued and paid out vacation time earned in 2010 before it even filed this formula rate petition. And in subsequent years, AIC notes it again will have accrued and paid out vacation time earned before its formula rates will be updated. AIC states it will always be behind on cash collections for this expense item, noting that there is no cookie jar of money financed by ratepayers that AIC is keeping for a rainy day. AIC submits that no 2010 accrued vacation expense will have been collected from ratepayers before the Commission's Order in this proceeding—well after AIC has paid this expense. AIC recommends that the Commission reject Staff, AG/AARP, and CUB's adjustment to deduct the amount of the accrual from rate base.

AIC notes that the Commission does not have a long-standing history of making this adjustment, as in both AIC's last gas rate case (Docket No. 11-0282) and last completed electric rate case (Docket Nos. 09-0306 et al. (Cons.)), the Commission did not make a deduction to rate base in the amount of the accrued liability for vacation pay. In each instance, AIC opines that the Commission also approved rates that included ADIT related to accrued vacation pay in rate base. AIC contends that no other prior AIC or legacy utility rate decisions in which this adjustment occurred have been identified, and in fact, parties can identify only one prior instance where the Commission has deducted the vacation liability balance from rate base – the recent ComEd formula rate proceeding. AIC urges the Commission to not make the same mistake twice and instead should find that the record in this proceeding demonstrates the accrued liability balance is not a free source of ratepayer supplied funds that must be deducted from rate base.

b. Staff Position

Staff notes that it and Intervenors have proposed an adjustment to treat the liability for accrued vacation pay, which represents a source of non-investor supplied capital, as an operating reserve and deduct it from rate base. Staff states that the operating reserve is offset by the related ADIT, which AIC included in rate base. Because the vacation pay accrual takes place in advance of payment, Staff avers there is a book-tax timing difference: vacation pay is only deductible for income tax purposes when it is paid. Staff states that AIC properly records ADIT to recognize the effect of this timing difference, while Intervenor witnesses posit that, if an ADIT debit balance is included in rate base, the related accrued liability should be included in the operating reserves deducted from rate base.

Staff notes that its adjustment is similar in some respects to AG/AARP witness Effron's adjustment. However, Staff's adjustment differs materially in the direct labor allocation factor chosen to calculate the electric portion of accrued vacation pay. Staff chose to use the direct labor allocation factor that includes administrative and general labor, whereas Mr. Effron chose to use the direct labor allocation factor that excludes administrative and general labor. Staff indicates that it now believes that the direct labor allocation factor that excludes administrative and general labor is the more accurate choice, as it is the allocation factor AIC used to calculate the electric portion of its 2010 Year End OPEB Liability. Therefore, the adjustment as proposed by Mr. Effron is adopted by Staff and reflected in Appendix A.

Staff states that it and Intervenors proposed a similar adjustment regarding accrued vacation pay in Docket No. 11-0721, ComEd's formula rate filing. In the Order entered May 29, 2012 in Docket No. 11-0721, Staff notes the Commission approved the adjustment to deduct accrued vacation pay from rate base. Staff suggests it is not aware of any differences between the facts regarding accrued vacation pay from the ComEd docket as opposed to the AIC docket that would warrant a different regulatory treatment. In order to maintain consistency in the formula rate filings and because accrued vacation pay represents a source of non-investor supplied capital, Staff suggests the Commission adopt the AG/AARP adjustment to treat AIC's liability for accrued vacation pay as an operating reserve and deduct it from rate base.

c. AG/AARP Position

AG/AARP note that in determining rate base, a utility must take into account the fact that not all of the expenses it accrues in a given time period will be paid out in that same time period. AG/AARP state the lag between accrual and payment must be taken into account in calculating the utility's CWC allowance, part of the investment upon which the utility will be granted a return. AIC explained that it accrues and expenses vacation pay in the year prior to that in which the employee actually receives payment, therefore AG/AARP contend this lag between accrual of vacation pay expense and the actual cash disbursement must be accounted for in determining AIC's rate base. AG/AARP suggest that the problem with AIC's accounting for accrued vacation pay is that AIC did not distinguish its treatment of accrued vacation pay expense, but instead implicitly included vacation pay in its calculation of CWC as part of total payroll expense, which carries a lag in payment not of a year, but of only 11.39 days. As AG/AARP witness Effron explains, because the source of all funds provided by the longer lag in payment of vacation pay is not implicitly recognized in AIC's calculation of CWC, AIC's rate base must be modified to reflect this lag. Mr. Effron suggests that AIC's accrued liability for vacation pay therefore should be treated as an operating reserve (an expense that has been accrued, but not yet paid) and deducted from rate base.

In addition, AG/AARP opine that AIC's rate base must be modified to correctly reflect the tax effects of the operating reserve balance that has been deducted from rate base. AG/AARP assert that AIC cannot deduct vacation pay expense for income tax purposes until that vacation expense is paid, therefore AIC's rate base must recognize the fact that accruals for vacation pay occur in advance of payment by recording deferred taxes, resulting in deferred tax debit balances that are included in rate base and that offset the accrued reserve balance deduction from rate base. AIC's deferred tax debit balances included in rate base should be calculated consistent with the accrued liability giving rise to those deferred taxes and deducted from rate base.

AG/AARP note that the cost of vacation pay recognized in 2010 was the full amount of vacation pay earned in that year, and not, as AIC has maintained, just the increment added to vacation pay liability in that year. AG/AARP state that AIC accrued vacation pay applicable to jurisdictional electric delivery services for 2010 in the amount of $11,834,000 as vacation pay was earned, and reversed vacation pay applicable to electric delivery services in the amount of $11,478,000, as vacation pay earned in 2009 was paid out. Of this $11,834,000, AG/AARP claim $675,000 was recognized in AIC's CWC allowance, so the difference of $11,159,000 should be treated as an operating reserve and deducted from rate base.

Additionally, AG/AARP claim that AIC's related deferred tax debit balance included in rate base should be modified so that it is consistent with the balance that is deducted from rate base. Based on a combined income tax rate of 39.745%, AG/AARP state that AIC's deferred tax debit balance in connection with its 2010 accrued vacation pay is $4,703,000 ($11,834,000 X .39745 = 4,703,000), which is $547,000 less than the year-end deferred tax debit balance of $5,250,000 reflected on AIC Ex. 13.2, Workpaper 4. Thus AG/AARP believe that AIC's deferred tax debit balance should be reduced by the $547,000.

AG/AARP submit that the appropriate treatment of AIC's accrued vacation pay results in a deduction to rate base of $11,159,000 (operating reserve for an expense item that has accrued but not yet paid) plus $547,000 (the difference between AIC's deferred tax debit balance and the proper deferred tax debit balance), for a total rate base deduction of $11,706,000.

d. CUB Position

Though AIC included in rate base ADIT on Vacation Pay, CUB claims AIC did not properly take Accrued Vacation Pay into account in determining rate base. Initially, CUB notes that AIC did not account for the vacation pay accrual in any way. CUB witness Smith testified that, though one way of addressing the lag in payment of vacation pay could be to reflect a very long lag in the lead-lag study, the more appropriate method of adjusting AIC's rate base to account for accrued vacation liability is to treat the balance as a direct offset to rate base. On rebuttal, CUB states that while AIC amended its lead-lag study to reflect vacation accrual, this adjustment is not adequate. Rather than deducting the accrued vacation balance from rate base, as Mr. Smith recommended, CUB avers that AIC made an adjustment to the payroll expense lead. CUB argues, however, that AIC's own rebuttal presents reasons for not including the vacation accrual in the lead-lag study.

CUB opines that the basic matching principal requires that if the related ADIT debit balances are included in rate base, then the accrued liabilities giving rise to those deferred balances should be included in the operating reserves deducted from rate base. CUB notes the Commission addressed this same issue in ICC Docket 11-0721, where the Commission stated, "While ComEd argues that any accrued vacation pay is short-term in nature, Staff, AG/AARP, CUB/City all point out that the balance on this item remains constant from one year to the next, due to the fact that, as ComEd's employees use vacation pay, they accrue more vacation pay." (Order at 69-70) CUB avers that the Commission ultimately concluded that the accrued vacation is a source of funds (i.e., a source of capital) for the utility and should be reflected as a reduction to rate base. CUB submits that no evidence has been presented in this docket to conclude otherwise; therefore the Commission should adopt CUB's proposed adjustment of $13.205 million.

e. Commission Conclusion

The Commission notes that vacation pay is an accrued expense recorded on a company balance sheet, which accrual represents the liability existing on the company books associated with vacation time earned by employees. Like other accrued expenses, it appears that AIC notes that the expense is recorded for employee services before compensation is paid, and, as a result, there is a lag between the time vacation pay is accrued and the time the expense is paid.

It appears to the Commission that Staff, AG/AARP and CUB each seek to deduct the amount of the accrued vacation pay at 2010 year-end from rate base. AIC asserts that it properly reflected vacation pay in its CWC calculation. AIC submits that it properly included the ADIT balance in rate base without making a deduction for the accumulated liability balance. AIC notes that the Commission does not have a long history of making this adjustment, indicating that in AIC's last gas rate case, Docket No. 11-0282, and AIC's last combined rate case, Docket Nos. 09-0306 et al. (Cons.), the Commission did not make a deduction to rate base in the amount of the accrued liability for vacation pay. While AIC recognizes that the Commission did adopt this adjustment in ComEd's smart grid docket, Docket No. 11-0721, AIC urges the Commission to find that the record in this proceeding demonstrates that the accrued liability is not a free source of ratepayer supplied funds that must be deducted from rate base.

Staff appears to have originally proposed an adjustment different from the various Intervenors on this issue; however, in its Briefs it appears that Staff now supports the proposed adjustment of AG/AARP on accrued vacation pay. Staff notes that a similar adjustment was proposed and adopted in Docket No. 11-0721, and Staff indicates that it is not aware of any differences between the facts in the two dockets that would warrant a different regulatory treatment.

AG/AARP argue that AIC's accrued liability for vacation pay should be treated as an operating reserve, an expense that has been accrued but not yet paid, and deducted from rate base. AG/AARP also assert that AIC's rate base must be modified to correctly reflect the tax effects of the operating reserve balance that has been deducted from rate base. The Commission notes that AG/AARP believe the appropriate treatment of AIC’s accrued vacation pay results in a deduction to rate base of $11,159,000 (operating reserve for an expense item that has accrued but not yet paid) plus $547,000 (the difference between AIC’s deferred tax debit balance and the proper deferred tax debit balance), for a total rate base deduction of $11,706,000.

CUB opines that the basic matching principal requires that if the related ADIT debit balances are included in rate base, then the accrued liabilities giving rise to those deferred balances should be included in the operating reserves deducted from rate base. CUB notes the Commission addressed this same issue in Docket No. 11-0721, in which the Commission ultimately concluded that the accrued vacation is a source of funds (i.e., a source of capital) for the utility and should be reflected as a reduction to rate base. CUB submits that no evidence has been presented in this docket to conclude otherwise; therefore the Commission should adopt CUB's proposed adjustment of $13.205 million.

The Commission finds that the proposed adjustment of AG/AARP, as endorsed by Staff, results in the proper ratemaking treatment of this item. It appears to the Commission that there is no discernible difference between this proceeding and Docket No. 11-0721 that would properly result in disparate rate making treatment of the same item between the two dockets. The Commission therefore adopts AG/AARP's proposed adjustment that results in a total deduction to rate base of $11,706,000.

5. Account 190 Asset – Unamortized ITCs

a. AIC Position

AIC notes that both AG/AARP and CUB recommend rate-base reductions tied to items contained in Account 190. Both parties assert that the unamortized balance of investment tax credits (“ITC”) should be removed, while AG/AARP alone recommend removing what it calls the "step-up basis metro." AIC contends that these recommendations are asymmetrical, lack merit, and should be rejected.

AIC avers that prior to Docket No. 11-0282; AIC neither recognized the amortization of ITCs as a reduction to income tax expense nor included any of the corresponding ADIT assets in rate base. Based on AG/CUB's recommendation in that docket, AIC indicates that it now recognizes ITCs in both categories: by reducing expenses and including the corresponding ADIT balance in rate base. AIC states that neither AG/AARP nor CUB opposes the reduction to expenses, but both recommend removing the corresponding asset from rate base.

AIC notes that AG/AARP recommend that the deferred tax item labeled unamortized ITC be eliminated from the determination of the balance of ADIT deducted from plant in service in the calculation of AIC's delivery services rate base. While AG/AARP recognize that the amortization of ITCs is reflected as a credit to income tax expense and reduces AIC's revenue requirement, AIC notes that AG/AARP nevertheless contend that since the deferred ITC itself is not deducted from rate base, the deferred tax debit balance that arises from that deferred ITC should not be added to rate base.

AIC argues that this recommendation must be rejected as asymmetrical, contending that AG/AARP want to keep a benefit of reduced income tax expense, but wishes to ignore the asset from which the benefit arises. AIC argues that the fact that the benefit is recognized through reduced expense provides no basis for also reducing rate base, but is rather why the asset must be recognized. AIC states the expense reduction is funded by the tax credits, so those assets must be recognized.

AIC agrees with AG/AARP that the amortization of the ITC was actually recorded on AIC's books in 2010 but that the deferred tax item in Account 190 does not arise from the amortization of ITC. AIC states that, by definition, the unamortized balance cannot "arise from" amortization because it is an unamortized balance, noting that amortization reduces the unamortized balance; it does not create it. AIC contends this does not show that the unamortized balance does not belong in rate base.

While AG/AARP assert that this treatment was adopted in Docket No. 11-0721, AIC submits this provides no support for its recommendation as this issue was not actually litigated in that case, and the bare fact that another utility proposed different treatment in another, complex case simply does not show that the adjustment is correct in this case. AIC asserts this is certainly correct where ComEd uses a different method of calculating income tax expense than AIC. Because AG/AARP support the ITC reduction to income tax expense, AIC argues the corresponding asset must also be recognized.

AIC also avers that CUB has provided no basis for its proposed reduction, noting that CUB witness Smith recommended this reduction, testifying that the ITC can be reflected for ratemaking purposes either as (1) a reduction to rate base by reflecting the accumulated deferred ITC balance as a deduction to rate base or (2) as a reduction to income tax expense by amortizing it ratably over the useful life of the plant to which it relates. AIC notes that according to Mr. Smith, under neither option is an amount added to utility rate base for unamortized ITC. AIC suggests that Mr. Smith actually proves AIC's point, which is that it would be improper to reduce both rate base and expense. AIC states that his first option for recognizing ITC (a reduction to rate base) assumes that the unamortized ITC balance is already part of rate base, as the balance cannot be removed from rate base unless it is there to begin with. As for the second option, AIC notes it recognizes ITC through reduced expenses, but it plainly does not, as CUB recommends, remove the balance from rate base; that is what the first option does. AIC argues that CUB essentially wants to check "all of the above" and use both options. AIC submits that CUB's proposal would remove the unamortized credits from rate base (Option 1) and recognize the credits through reduced expenses (Option 2), but this is not just asymmetrical, it double-counts the credits against AIC.

AIC notes that Staff, in its Initial Brief, has now reversed itself on its suggested treatment of this issue, and now supports eliminating the unamortized balance of ITCs from rate base. AIC states that Staff witness Hathhorn recommended rejecting CUB and AG/AARP's proposal to remove unamortized ITCs from rate base, explaining that AIC's approach is symmetrical and consistent with its latest Commission order. AIC submits that this testimony was never revised or corrected, although on the stand, Ms. Hathhorn made an ambiguous statement. At the time AIC adopted AG/CUB's proposed expense treatment (in the midst of a case last year), "the deferred asset was not in rate base, and so that would be a correction to the symmetrical—that would be a difference from the symmetrical treatment." (Tr. at 231, lines 4-7.) AIC suggests that what this statement means is unclear, and the ambiguity was never clarified. In response to an objection by AIC, however, counsel for Staff asserted that whatever Ms. Hathhorn meant, she was not correcting her direct testimony, in which she rejected the ITC adjustment on the grounds it was asymmetrical. Nevertheless, despite the contrary testimony of its own witness, AIC notes that Staff now asserts that the Commission "should accept the AG/AARP and CUB adjustment to rate base to remove [the unamortized ITC balance]." (Staff Initial Brief at 13)

While Staff claims that AIC has cited no authority other than its own on this issue, AIC alleges that even a cursory reading of AIC's testimony would show this not to be true. AIC submits that Mr. Stafford provided a detailed explanation of AIC's position on this issue in his testimony and that it is incorrect for Staff to ignore this.

Although Staff points out that when AIC initially accepted a reduction to income tax expense in Docket No. 11-0282, no deferred tax asset for ITCs was included in rate base; AIC argues that whatever happened in an earlier case does not, by itself, establish the appropriate ratemaking treatment. AIC submits that this is particularly true when the issue was not litigated. AIC notes that in Docket No. 11-0282, the ITC expense reduction was not proposed by AIC, but by other parties, and AIC accepted the adjustment during the proceeding. AIC contends that whether the adjustment was correctly implemented was not litigated in Docket No. 11-0282, and it notes that there is no long-standing historical practice applicable here. Along those lines, AIC notes that the case was filed last year. At best, AIC suggests the failure to include the ITC asset in rate base provided the other parties with a temporary windfall, but it does not cure the asymmetry problem nor mean that it can never be cured.

AIC opines that the question goes to correct treatment, and if the expense-reducing effect of the tax asset is going to be recognized, then the asset itself should be recognized as well. AIC argues that symmetry is a fundamental principle of ratemaking, and Staff, AG/AARP, and CUB's proposal runs afoul of it. (See, e.g., Docket No. 05-0597, 2006 Ill. PUC LEXIS 38, at *109-10 (May 4, 2006) (recognizing ratemaking principle of symmetry); Rulemaking to Implement Order 91-0050, Docket 92-0274, 1994 Ill. PUC LEXIS 472, at * (Nov. 22, 1994) (concluding that a certain proposed regulatory method "is flawed" because, inter alia, "it does not treat externalities symmetrically"; "[i]n any rational economic evaluation process, costs are offset with attendant or consequential benefits"). As AIC has explained, the proposal to remove the deferred tax asset from rate base is asymmetrical: it recognizes the tax benefit through a reduction to expense, yet removes the benefit-generating asset from rate base. AIC submits that one or the other is fair, but not both.

To the extent CUB and AG/AARP fault AIC for not recognizing the ITC offsets solely through rate-base adjustments, AIC suggests they have not considered the effect this would have. As Mr. Stafford explained on cross-examination, under either option offered, recognizing the offset as a reduction to expense or to rate base, there would be a deferred tax asset recorded. Under AIC's proposal, however, the approximate impact on revenue requirement is negative one million dollars, while under the other approach; there would actually be a net increase in revenue requirement. AIC contends that while either option recognizes the deferred tax asset, AIC selected the option that resulted in lower rates.

b. Staff Position

Staff recommends that the Commission accept the AG/AARP and CUB adjustment to rate base to remove inclusion of a deferred tax asset related to AIC's past ITCs since the Commission has never previously allowed AIC a return on such asset. Staff indicates that AIC is correct that in Docket No. 11-0282, it changed its presentation of ITCs, based upon an AG/CUB recommendation, such that a deduction was made to income tax expense for amortization of ITCs. Staff states the record also shows that, in Docket No. 11-0282, no deferred tax asset for ITCs was included in rate base. Staff notes that AG/AARP argue that, if the deferred ITC is not deducted from rate base, then the deferred tax debit (or asset) balance that arises directly from that deferred ITC should not be added to rate base; i.e., the treatment should be consistent. Staff agrees with this conclusion. Staff asserts AIC cites to no authority other than its own opinion that it believes it is appropriate to include the deferred tax asset in rate base since it now flows through the amortization of the ITC to ratepayers. Staff recommends the Commission reject AIC's self-serving adjustment based only on its beliefs and instead use sound, consistent principles to treat the deferred ITC credits and tax assets consistently by including neither amount in rate base.

c. AG/AARP Position

AG/AARP note that ADIT represent the cumulative effect of income tax assets or liabilities recorded on temporary differences between book income and taxable income. AG/AARP witness Effron analyzed the balances of ADIT deducted from utility plant in service in the determination of AIC's rate base and concluded that certain adjustments to Account 190 are necessary to properly reflect the ADIT debit balance and the corresponding deductions to AIC's rate base for purposes of setting rates. Mr. Effron proposes adjustments related to three items included in Account 190: unamortized ITC, tax depreciation step-up basis Metro, and deferred compensation. AG/AARP state that each of these items is an ADIT debit balance, and as the net ADIT on AIC Exhibit 2.1 is a credit balance that is deducted from plant in service in the determination of rate base, AIC's inclusion of these debit balances in the total ADIT has the effect of reducing the net rate base deduction for ADIT.

AG/AARP aver that the balance of ADIT related to unamortized ITCs represents the electric distribution portion of ADIT on federal ITCs. They state that deferred ITCs represent tax savings that AIC has realized but has not recognized as income. Because of certain provisions of the IRC, AG/AARP note the deferred ITCs cannot be deducted from rate base, although it does represent non-investor supplied funds. They note the deferred ITC is shown as a liability on AIC's balance sheet, but is not deducted from rate base; while the ADIT debit balance in Account 190 is, in effect, an offset to the ITC liability. AG/AARP state that AIC explained that it includes this item in its delivery service rate base since the underlying assets giving rise to the tax deferral are included in rate base and amortization of ITCs benefits ratepayers in the calculation of income tax expense, AIC believes it is appropriate to include the jurisdictional portion of this deferred tax in AIC's rate base. AG/AARP contend that this explanation does not justify inclusion of the deferred income tax balance related to the unamortized ITCs in rate base. As noted by Mr. Effron, while it is correct that the amortization of ITCs is reflected as a credit to income tax expense in the calculation of AIC's revenue requirement, the deferred ITC itself is not deducted from AIC's delivery services rate base. If the deferred ITC is not deducted from rate base, then they submit that the deferred tax debit balance that arises directly from that deferred ITC should not be added to rate base. In accordance with this analysis, Mr. Effron recommended that the deferred tax item labeled unamortized ITC should be eliminated from the determination of the balance of ADIT deducted from plant in service in the calculation of AIC's delivery services rate base. AG/AARP note that elimination of this item increases the net balance of ADIT by $3,423,000 and decreases AIC's rate base by the same amount.

AG/AARP claim that the reduction of income tax expense for the amortization of the ITC is not an adjustment to test year expenses, but that the amortization of the ITC was actually recorded on AIC's books in 2010 and reduced the net income tax accordingly. AG/AARP note that AIC reflected the effect of this item in its calculation of net income tax expense, which did not require any adjustment to the actual expense. AG/AARP state that the deferred tax item in Account 190 does not arise from the amortization of ITC. They argue that it instead arises from the deferred credit balance of ITC on AIC's balance sheet, which represents realized tax savings which have not yet been reflected in the income statement. AIC does not dispute this simple fact. As the deferred credit balance of ITC is not deducted from AIC's rate base, the directly related deferred tax debit balance should not be included in the net balance of ADIT and used to increase AIC's rate base.

AG/AARP note that the Account 190 deferred tax debit balance related to ITC was explicitly excluded from the determination of the delivery services rate base by ComEd in Docket No. 11-0721, although the amortization of ITC was credited to income tax expense in that case. AG/AARP state that this treatment was not disputed by any of the parties and was accepted by the Commission in the determination of the revenue requirement in that case.

For these reasons, AG/AARP submit that Mr. Effron's proposed elimination of the deferred tax item labeled unamortized ITC from the determination of the balance of ADIT deducted from plant in service in the calculation of AIC's delivery services rate base should be adopted.

d. CUB Position

CUB asserts that AIC has failed to meet its burden to demonstrate that unamortized ITC should be added to its rate base. In accordance with normalization requirements, CUB notes that ITC can be reflected for ratemaking purposes either as (1) as a reduction to rate base by reflecting the accumulated deferred ITC balance as a deduction to rate base or (2) as a reduction to income tax expense by amortizing it ratably over the useful life of the plant to which it relates. CUB suggests that either of these methods is appropriate and provided for under the IRC and Treasury Regulations as accepted normalization methods to reflect ITC for ratemaking purposes. CUB states that the accounting and ratemaking treatment for ITC is largely dictated by former IRC Sections 46(f)(1) and 46(f)(2). CUB opines that the IRC permits sharing of ITC benefits between utility investors and customers either by: (1) deducting ITC from rate base, and not reflecting an impact on income tax expense; or (2) reflecting ITC is as a reduction to income tax expense by amortizing it, thus not reflecting a deduction (and no increase) to rate base for any deferred ITC balance.

CUB notes that under neither option is an amount added to the utility's rate base for unamortized ITC. CUB believes that as AIC has chosen to reduce income taxes for ITC amortization, there is no basis for either adding or deducting the ITC from rate base. CUB suggests that under neither method for normalizing ITC for utility ratemaking purposes under former IRC Section 46(f)(1) and 46(f)(2) is an amount of ITC added to utility rate base. CUB argues that AIC has provided no valid basis for adding the deferred ITC to jurisdictional rate base, and avers that removal of the

Accumulated Deferred ITC that AIC had proposed to include in rate base reduces AIC’s proposed jurisdictional rate base by $3.423 million.

e. Commission Conclusion

AIC avers that prior to Docket No. 11-0282, AIC neither recognized the amortization of ITCs as a reduction to income tax expense nor included any of the corresponding ADIT assets in rate base. Based on AG/CUB’s recommendation in that docket, AIC indicates that it now recognizes ITCs in both categories: by reducing expenses and including the corresponding ADIT balance in rate base. AIC states that neither AG/AARP nor CUB opposes the reduction to expenses, but both recommend removing the corresponding asset from rate base.

AIC argues that this recommendation must be rejected as asymmetrical, contending that AG/AARP want to keep a benefit of reduced income tax expense, but wishes to ignore the asset from which the benefit arises. AIC argues that the fact that the benefit is recognized through reduced expense provides no basis for also reducing rate base, but is rather why the asset must be recognized. AIC states the expense reduction is funded by the tax credits, so those assets must be recognized. AIC notes that while this treatment was adopted in Docket No. 11-0721, it does not appear that this issue was actually litigated in that docket, and the mere fact that another utility proposed different treatment of an issue does not show that the treatment is correct in this case.

The Commission notes that Staff initially supported AIC's recommendation on this issue; however, upon further analysis of evidence discovered post testimony and discussed at the hearings, Staff now recommends the Commission accept the AG/AARP and CUB adjustment to rate base so as to remove inclusion of a deferred tax asset related to AIC's past ITCs. Staff argues the Commission has never allowed a return on such an asset, and indicates that the record in Docket No. 11-0282, AIC's last gas rate case, shows that no deferred tax asset for ITCs was included in rate base.

AG/AARP recommend that the deferred tax item labeled unamortized ITC should be eliminated from the determination of the balance of ADIT deducted from plant in service in the calculation of AIC’s delivery services rate base. AG/AARP note that elimination of this item increases the net balance of ADIT by $3,423,000 and decreases AIC’s rate base by the same amount. AG/AARP contend that there is no justification for inclusion of the deferred income tax balance related to the unamortized ITC in rate base. AG/AARP suggest that if the deferred ITC is not deducted from rate base, then the deferred tax debit balance that arises directly from that deferred ITC should not be added to rate base.

CUB also asserts that AIC has failed to meet its burden to demonstrate that unamortized ITC should be added to its rate base. CUB opines that the IRC permits sharing of ITC benefits between utility investors and customers either by: (1) deducting ITC from rate base, and not reflecting an impact on income tax expense; or (2) reflecting ITC is as a reduction to income tax expense by amortizing it, thus not reflecting a deduction (and no increase) to rate base for any deferred ITC balance. CUB notes that under neither option is an amount added to the utility's rate base for unamortized ITC.

The Commission agrees with AG/AARP and CUB as to the appropriate treatment of this item. For the reasons set forth by AG/AARP and CUB, the Commission finds that the proposed adjustment they suggest is appropriate and it will be adopted for purposes of this proceeding.

6. Account 190 Asset – Step-Up Basis Metro

a. AIC Position

AIC notes that AG/AARP recommend an additional rate-base reduction related to Account 190. AIC states that according to Mr. Effron, in 2005 AmerenUE transferred certain tax depreciable assets to AmerenCIPS; which transfer occurred at the book value of the assets, which was higher than the tax basis of those assets at that time. AIC notes that Mr. Effron claims that since the transfer did not result in any payment of taxes, it should not result in an increase in the net value of those assets included in AIC's rate base. AIC suggests that the error in Mr. Effron's recommendation is that it assumes that the transfer would, in fact, result in any return of additional funds to AIC. AIC asserts, however, that the transfer had zero effect on rate base and notes that Staff agrees that the evidence showed that the ADIT included in rate base from this purchase is zero. AIC argues that since the net effect is zero, no adjustment is necessary. In confirmation, AIC notes that Staff witness Hathhorn testified that during the original transfer case the credit entry to account 190 of $17,664,689 was offset by a debit entry to account 282 of $17,664,689.

AIC suggests that the problem is that Mr. Effron focuses exclusively on one item, when that item was only one part of the accounting necessary to accommodate AmerenCIPS' purchase of AmerenUE's assets. AIC avers that when AmerenCIPS purchased the AmerenUE property, it did so at net book value, so no book-tax difference and no ADIT resulted; however, AmerenUE's records reflected the book value of the assets, depreciation reserve, and ADIT. AIC submits that to account for the overall lack of book-tax difference, AmerenCIPS set up a corresponding "contra-deferred tax liability" in Account 190 so that net deferred taxes at the date of the purchase on AmerenCIPS books was zero.

AIC claims that Mr. Effron is attempting to zero out an ADIT entry that has already been zeroed out, therefore AG/AARP's recommendation would result in double counting. AIC asserts the step-up-basis item in Account 190, which Mr. Effron recommends offsetting by a reduction to rate base, is already offset by an equal amount of credit balance of ADIT in Account 282. AIC opines that making AG/AARP's reduction would not correct any error. Instead, they argue that it would commit one by understating rate base.

AIC notes that Mr. Effron offers no response to this issue in rebuttal, but simply reiterated his previous position. AIC suggests that this simply ignores the fact that the only challenged entry has already been zeroed out. AIC opines that Mr. Effron's rebuttal testimony does not acknowledge this issue and hence offers no justification for adopting his asymmetrical recommendation.

AIC notes that AG/AARP brought up a new argument in its Initial Brief, contending that AIC "booked income . . . and is now seeking to have ratepayers pay a return on the asset that was recorded in associate [sic] with that income." (AG/AARP Initial Brief at 48) AIC suggests there are numerous problems with this argument. AIC submits that procedurally, this argument is waived as it was not raised until after the hearing, and it also lacks necessary record support. Moreover, AIC alleges it is plainly dependent on a selective reading of the facts and is contradicted by the record.

b. Staff Position

Staff recommends the Commission reject the AG/AARP adjustment to remove a deferred tax asset recorded at the time of AmerenCIPS' purchase of certain depreciable assets from AmerenUE. Staff believes that AIC has demonstrated that the adjustment is improper since net ADIT included in rate base from this asset purchase is zero. Since the net effect to ADIT of the transaction is zero, Staff opines that no adjustment is necessary.

c. AG/AARP Position

AG/AARP note that Mr. Effron proposed an adjustment related to an item included in Account 190 identified as Tax Depreciation Step-up Basis Metro. AG/AARP state that this ADIT balance represents certain tax depreciable assets that were transferred in 2005 by AmerenUE to AmerenCIPS, according to AIC. AG/AARP state the transfer took place at the book value of the assets, which at the time of the transfer was higher than the tax basis, and because the transfer of the assets was between affiliated members of a consolidated tax return, there was no gain for tax purposes at the time of the transfer. AG/AARP claim that AmerenCIPS "stepped up" the tax basis of the assets to their book value at the time of the transfer. AG/AARP aver that with the book basis equal to the tax basis, there would be no net deferred taxes, and AmerenCIPS recorded a deferred tax asset that offset the related accumulated deferred taxes at the time of the asset transfer.

AG/AARP argue, however, that the balance of ADIT related to "tax depreciation step-up basis Metro" should not be includable in AIC's rate base. Mr. Effron testified that the transfer of the assets from AmerenUE to AmerenCIPS at book value did not result in any payment of taxes at the time of the transfer, and this transfer of property from one regulated utility to another should not result in any increase to the net value of those assets included in AIC's rate base. For ratemaking purposes, AG/AARP assert the ADIT associated with the assets at the time of the transfer should follow the assets, without any offset.

AG/AARP note the deferred tax debit balance is, in effect, an offset to an income tax expense that was not actually paid. As this item did not require any actual outlay of investor funds, AG/AARP argue that it should not be included in AIC's rate base. AG/AARP claim that elimination of the state and federal deferred ADIT on "tax depreciation step-up basis Metro" reduces AIC's jurisdictional rate base by $7,057,000 (Schedule DJE-1.1).

AG/AARP note that AIC contests this adjustment, arguing that because AmerenCIPS acquired the relevant property from AmerenUE at net book cost, the book cost of the property was the same as the tax basis to AmerenCIPS at the time of the acquisition, and thus there was no book-tax difference and no ADIT for AmerenCIPS at the time of the acquisition. AG/AARP suggest that AIC's argument on this point is not persuasive.

As Mr. Effron explained, there were related ADIT on the books of AmerenUE at the time of the sale, as Mr. Stafford acknowledges. AG/AARP opine that ADIT balance should follow the assets, without any entry to Account 190 to offset the credit balance of ADIT. Otherwise, AG/AARP complain the net rate base value of the assets would be higher in the hands of AmerenCIPS than the net rate base value of the assets in the hands of the affiliate from whom the assets were purchased, which would clearly be inappropriate.

AG/AARP claim that it was established during cross-examination that the offsetting entries at the time that the deferred tax assets were established was to income, rather than rate base. In other words, AG/AARP state that AIC booked income at the time of the transfer and is now seeking to have ratepayers pay a return on the asset that was recorded in association with that income. AG/AARP argue that AIC should not have booked a gain on the transfer of assets between affiliates and that customers should certainly not be required to pay a return on an asset that was recorded in association with that gain. AG/AARP urge the Commission to adopt Mr. Effron's proposed adjustment.

d. CUB Position

CUB supports the adjustment proposed by AG/AARP witness Effron related to "tax depreciation step-up basis Metro." This ADIT balance is the result of the 2005 transfer of AmerenUE tax depreciable assets to AmerenCIPS; a transfer that did not result in any payment of taxes at the time of the transfer, and which did not result in any increase to the net value of those assets included in AIC's rate base. There were related ADIT on the books of AmerenUE at the time of the sale. For ratemaking purposes, the ADIT associated with the assets at the time of the transfer should follow the assets, without any offset. If there is no entry to Account 190 to offset the credit balance of ADIT, the net rate base value of the assets would be higher in the hands of

AmerenCIPS than the net rate base value of the assets in the hands of the affiliate from whom the assets were purchased - clearly an inappropriate result. Therefore, the Commission must make an adjustment of $7.057 million.

e. Commission Conclusion

The Commission recognizes that AG/AARP recommend an additional rate-base reduction related to Account 190. According to Mr. Effron, in 2005 AmerenUE transferred certain tax depreciable assets to AmerenCIPS. That transfer occurred at the book value of the assets, which was higher than the tax basis at that time. AG/AARP claim that AmerenCIPS “stepped up” the tax basis of the assets to their book value at the time of the transfer. AG/AARP aver that with the book basis equal to the tax basis, there would be no net deferred taxes, and AmerenCIPS recorded a deferred tax asset that offset the related accumulated deferred taxes at the time of the asset transfer. AG/AARP argue, however, that the balance of ADIT related to “tax depreciation step-up basis Metro” should not be includable in AIC’s rate base.

AIC suggests that the error in Mr. Effron's recommendation is that it assumes that the transfer would, in fact, result in any return of additional funds to AIC. AIC asserts that the transfer had zero effect on rate base, and notes that Staff agrees that the evidence showed that the ADIT included in rate base from this purchase is zero, and since the net effect is zero, no adjustment is necessary. In confirmation, AIC notes that Staff witness Hathhorn testified that during the original transfer case the credit entry to Account 190 of $17,664,689 was offset by a debit entry to Account 282 of $17,664,689.

Staff recommends the Commission reject the AG/AARP adjustment, as Staff believes that AIC has demonstrated that the adjustment is improper since net ADIT included in rate base from this asset purchase is zero. Since the net effect to ADIT of the transaction is zero, Staff opines that no adjustment is necessary.

CUB supports the adjustment proposed by Mr. Effron related to “tax depreciation step-up basis Metro.” This ADIT balance is the result of the 2005 transfer of AmerenUE tax depreciable assets to AmerenCIPS; a transfer that did not result in any payment of taxes at the time of the transfer, and which did not result in any increase to the net value of those assets included in AIC’s rate base.

The Commission finds that AIC has properly accounted for these items, and, as recommended by Staff, no adjustment is necessary in this proceeding. The Commission therefore will reject the proposed adjustment of AG/AARP and CUB and find that no further adjustment is necessary to the Account 190 asset.

7. Construction Work In Progress Not Subject to AFUDC

a. AIC Position

AIC states that in their direct testimony, both Staff and AG/AARP proposed adjustments to AIC's requested level of Non-AFUDC construction work in progress ("CWIP") included in rate base. On rebuttal, AIC notes that it adopted Staff's proposal as the more appropriate of the two proposals. AIC claims that Staff's proposal is more transparent to the reader of the tariff in that it allows for CWIP to be included in year-end rate base but only to the extent the projects are not also counted in projected plant additions. AIC suggests that Staff's proposal also removes any potential for double counting, since the only portion of requested CWIP that would be included in Sch. FR B-1 rate base is the portion that is not included in projected additions. AIC contends that this adjustment also would not require the Commission to litigate in future rate proceedings whether any CWIP should be recovered under Section 9-214(e) of the Act.

AIC notes that on rebuttal, the AG started with the AIC and Staff agreed-upon reduced CWIP amount and proposed an additional adjustment to remove an additional project, claiming that this project was 100% financed by accounts payable balances. While AG/AARP claim investors provided none of the capital used to finance this project and thus the amount should not be included in rate base, AIC believes that Staff's proposal is the more appropriate adjustment to address the double-counting issue. On surrebuttal, AIC also indicated that, contrary to AG/AARP's assertion, the investment was financed by AIC well in advance of any recovery in rates of the dollars associated with this plant investment. AIC submits that AG/AARP adjustment to remove additional CWIP from rate base should be rejected.

b. Staff Position

Staff notes that AIC accepted Staff's adjustment in Schedule 1.10 for a deduction to rate base for specific project amounts duplicated in rate base, first in the balance of CWIP not subject to AFUDC and second in AIC's 2011 projected plant additions. AIC stated that Staff's adjustment is preferable to that proposed by AG/AARP. Staff further agrees that the cost of non-AFUDC CWIP should be included, although they suggest that it should be a component of the actual year's cost during the annual reconciliation. After further analysis of the record, Staff stated in its Reply Brief that the record supports AG/AARP's additional adjustment to exclude accounts payable associated with project 280082.

c. AG/AARP Position

AG/AARP state that among the projects for which AIC is requesting rate base recovery is a list of items that were included in its balance of CWIP but which were not earning AFUDC as of the end of the test year, December 31, 2010. Although AIC has removed some projects in response to a Staff-sponsored adjustment, AG/AARP argue that AIC's information still identifies that Accounts Payable remains as to several of these listed projects. AG/AARP claim that vendors, rather than shareholders, funded these CWIP investments as of year-end 2010, which means that AIC investors provided none of the capital used to finance these projects and they need not be excluded from rate base.

To properly remove that portion of the requested CWIP, AG/AARP witness Brosch quantified the adjustment needed to reduce AIC's asserted rate base for CWIP not subject to AFUDC that has not actually been funded by AIC investors. In response to information provided by AIC, AG/AARP's proposed adjustment is shown on AG/AARP Ex. 3.1, which starts with AIC's reduced CWIP amount and recognizes that the remaining projects were more than 100% financed by accounts payable balances, and therefore need not be included in rate base. AG/AARP assert that Mr. Brosch's adjustment is consistent with the Commission's recent determination in ComEd rate case Docket No. 10-0467 that CWIP should be properly reduced for Accounts Payable before being added to rate base:

> . . . It appears that there was no attempt on the part of ComEd to determine what, if any, of these smaller projects are funded by the lag between the time when they are booked and when the bills for these items/payment to employees or contractors are actually paid. As the AG and CUB point out, many of these items can be temporarily financed by time. Additionally, the AG asserts that ComEd's lead/lag study does not include CWIP-related items and ComEd's evidence provides no specifics indicating that the AG or Mr. Brosch are wrong in this regard.
>
> While Ms. Houtsma's testimony in this regard is vague, the Commission cannot conclude that it is inadmissible as a matter of law. (e.g., Fraley v. City of Elgin, 251 Ill. App. 3d 72, 76-77, 621 N.E.2d 276 (2nd Dist. 1993), discussing when factual conclusions are totally unsupported factually, and therefore may be disregarded, as a matter of law). $12.6 million is at issue, and it concerns many, many, small projects that can be completed quickly. The Commission also cannot state, within a reasonable degree of certainty, that all of these projects are vendor-financed. The Commission appreciates the fact that accrual-based accounting records record items that will become due and owing in the future, as opposed to when the bills for those projects become due and owing. The Commission also appreciates the fact that there can be a lag between when work is performed and when the bill for that work is paid. However, without evidence indicating that these two lags allow ComEd to pay for its CWIP-related projects, the Commission cannot state, within a reasonable degree of certainty, that ComEd's CWIP-related projects are financed by these two lags.
>
> However, in ComEd's next rate case, any lead/lag study shall include the effect of accrual accounting on payment for its smaller CWIP-related payments (the payments that are at issue here and that are not

> accounted for with AFUDC). Failure to do so could result in a determination that ComEd did not meet its burden of proof, or, that ComEd failed to comply with a Commission Order, with all of the penalties that are provided for such failure in the Public Utilities Act.
> (Docket No. 10-0467, May 24, 2011 Order at 30-31)

AG/AARP aver that AIC witness Stafford indicated he was unaware of this recent CWIP decision in Docket No. 10-0467, although he did acknowledge that the utility's proposed CWIP projects in this case may include charges from vendors that remained in Accounts Payable at year end 2010. AG/AARP note that Mr. Stafford argues that these projects should be included anyway, because the CWIP amounts were ultimately paid outside of the test year period and that the amounts in question were paid in 2011.

AG/AARP assert that the evidence is clear that vendors, and not shareholders, have funded certain projects identified as CWIP in AIC's rate base presentation. AG/AARP urge the Commission to accept Mr. Brosch's adjustment to remove CWIP projects from rate base that were more than 100% financed by accounts payable balances.

d. CUB Position

CUB supports the adjustment of Mr. Brosch to reduce the CWIP allowed into rate base for related Accounts Payable balances. CUB states that this adjustment is consistent with the Commission's Order in Docket No. 10-0467, where the Commission found that short-term CWIP projects can be, and often are, funded by the lag between the time when they are booked and the time that the bills for these items are actually paid. (See Docket No. 10-0467, May 24, 2011 Order at 30). CUB avers that as this means that vendors, rather than shareholders, have funded these CWIP investments, therefore CUB supports the adjustment proposed by Mr. Brosch to adjust AIC's rate base by $241,000.

e. Commission Conclusion

It appears to the Commission that both AG/AARP and Staff proposed adjustments to AIC's requested level of non-AFUDC CWIP included in rate base. Each is proposing a different adjustment for this item. CUB indicates that it supports the proposed AG/AARP adjustment.

Staff notes that AIC accepted Staff's adjustment for a deduction to rate base for specific project amounts duplicated in rate base, first in the balance of CWIP not subject to AFUDC and second in AIC's 2011 projected plant additions. Staff further agrees that the cost of non-AFUDC CWIP should be included, although as a component of the actual year's cost during the annual reconciliation.

AIC indicates that it adopted Staff's original proposal as the more appropriate of the two proposals. AIC claims that Staff's original proposal is more transparent to the reader of the tariff in that it allows for CWIP to be included in year-end rate base but only to the extent the projects are not also counted in projected plant additions.

AG/AARP argue that among the projects for which AIC is requesting rate base recovery is a list of items that were included in its balance of CWIP, but which were not earning AFUDC as of the end of the test year, December 31, 2010. Although AG/AARP recognize that AIC has removed from rate base some projects in response to a Staff-sponsored adjustment, AG/AARP argue that AIC still includes in rate base a project funded through Accounts Payable. AG/AARP claim that vendors, rather than shareholders, funded this CWIP investment as of year-end 2010, which means that AIC investors provided none of the capital used to finance this project. Because the project was financed through Accounts Payable, AG/AARP insist that it needs to be excluded from rate base.

CUB indicates that it supports the proposed AG/AARP adjustment, Further, in its Reply Brief, Staff opined that the Commission should adopt the AG/AARP proposed adjustment. Staff agreed that the record shows that the remaining project included in CWIP not subject to AFUDC (after Staff's adjustment was accepted by AIC) still contains amounts representing Accounts Payable which are vendor financed. Therefore, Staff recommended the additional AG/AARP adjustment be adopted by the Commission.

First, the Commission agrees that Staff's original adjustment to remove projects duplicated in projected plant and CWIP not subject to AFUDC is reasonable and is adopted by the Commission. Next, the Commission agrees with Staff and AG/AARP that the additional adjustment to remove Accounts Payable associated with the remaining project included in CWIP not subject to AFUDC is necessary since such vendor financing is not a shareholder cost that needs a rate base return. This conclusion is also consistent with the Commission's treatment of a similar issue in Docket No. 11-0721.

8. Average Rate Base – Projected Plant/ADR/ADIT

The parties to this proceeding have spent considerable time arguing whether average or year-end rate base should be used in calculating rates under Public Acts 97-0616 and 97-0646. Because this issue reflects an aspect of the formula implementation, this issue is discussed and resolved in Section X.B.6, below.

VI. OPERATING REVENUES AND EXPENSES

A. Uncontested Issues

1. Adjustment for Athletic Ticket/Event Expenses

AG/AARP and CUB recommend an adjustment to remove costs for athletic tickets and events. Staff also recommends disallowing these athletic event expenses through an adjustment to Account 930.1 - Corporate Sponsorships. AIC agrees with such an adjustment and recommends an amount of $128,649. AG/AARP, CUB, and Staff concur with this amount. The Commission finds this agreed-to adjustment removing costs for athletic tickets and events appropriate and adopts it.

2. Adjustment for Contributions to Political Groups/Quincy Gems

AG/AARP, CUB, and Staff recommend the disallowance of charitable contributions to organizations that are political in nature as well as a donation to the Quincy Gems Baseball organization. AIC is amenable to these adjustments, which are now reflected in its proposed revenue requirement (as reflected in its Initial Brief). The Commission finds these adjustments appropriate and adopts them.

3. Adjustment for EEI Memberships Dues Allocated to Lobbying

AG/AARP, CUB, and Staff recommend an adjustment to remove from the revenue requirement the portion of AIC's Edison Electric Institute association dues allocable to lobbying activities. AIC accepts this disallowance. The Commission finds this adjustment appropriate and adopts it.

4. Correction for Previously Disallowed Depreciation Expense

In response to Staff DR BAP 4.05, AIC agrees to reflect a correction to previously disallowed depreciation expense on production related pension and OPEB costs. The Commission concurs that this correction is appropriate and adopts it.

B. Contested Issues

1. Section 9-227 Donations/Charitable Contributions

Section 9-227 of the Act provides in its entirety:

> It shall be proper for the Commission to consider as an operating expense, for the purpose of determining whether a rate or other charge or classification is sufficient, donations made by a public utility for the public welfare or for charitable scientific, religious or educational purposes, provided that such donations are reasonable in amount. In determining the reasonableness of such donations, the Commission may not establish, by rule, a presumption that any particular portion of an otherwise reasonable amount may not be considered as an operating expense. The Commission shall be prohibited from disallowing by rule, as an operating expense, any portion of a reasonable donation for public welfare or charitable purposes.

Whether donations to various organizations should be recoverable from ratepayers has recently become a contested issue in rate cases. The Commission considered this issue in both Docket No. 11-0282 pertaining to AIC's last gas rate case and Docket No. 11-0721 relating to ComEd's first formula rate case. In the latter docket, the Commission directed that a rulemaking be initiated to facilitate determining which donations should be recoverable from ratepayers. On July 31, 2012, the Commission initiated the rulemaking, which is Docket No. 12-0457.

a. Staff Position

Staff reads Section 9-227 as recognizing four types of potentially recoverable donations; those made for (1) the public welfare, (2) charitable scientific purposes, (3) charitable religious purposes, and (4) charitable educational purposes. Staff views the latter three as having fairly obvious meanings, but views the first as more ambiguous. To help determine when a donation made for the public welfare is recoverable, Staff turns to the IRC provision concerning tax exempt organizations. Section 501(c)(3) of 26 United States Code 1 et seq. sets forth the criteria that an organization must meet in order for it to be considered tax exempt in the eyes of the federal government. Section 501(c)(3) states in full,

> (3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Organizations described in Section 501(c)(3) are commonly referred to as charitable organizations. Donations to such organizations are tax deductible on the donor's federal income tax return. In this proceeding, Staff recommends that the following contributions be disallowed and excluded from rates because they do not fit under any of the four categories of recoverable contributions: (1) donations made to community and economic development organizations and animal wellness groups which are not Section 501(c)(3) organizations and (2) a donation to the Illinois High School Association ("IHSA") (which is a Section 501(c)(3) organization) that was not for an educational purpose but in support of the state football playoffs.

Staff is comfortable relying on the generally understood meanings of "scientific," "religious," and "educational," but believes that the guidance provided by Section 501(c)(3) would be quite beneficial in applying the "public welfare" language of Section 9-227 of the Act. To begin with, Staff maintains that the disallowance of donations to organizations which are not Section 501(c)(3) organizations is appropriate because this accounting treatment is consistent with AIC's own policy concerning charitable contributions and because it is consistent with prior Commission practice. Staff explains that AIC has a policy of seeking recovery from customers only for those donations made to Section 501(c)(3) organizations. According to Staff, AIC has not followed its own internal policy concerning donations made for the public welfare which are not tax deductible. Staff contends further that in ComEd's formula rate case, the Commission's analysis and conclusion concerning charitable contributions implied that only tax-deductible charitable contributions may be included in rates. (See Docket No. 11-0721, May 29, 2012 Order at 98) Moreover, Staff continues, in the minutes for the Special Open Meeting on May 29, 2012 where Docket No. 11-0721 was discussed and decided, the Commissioners presumed that only Section 501(c)(3) organizations were being considered for recovery. (Special Open Meeting Minutes at 31) Staff also points out that the Order in Docket No. 11-0721 goes on to say that, “The Commission agrees with CUB/City's observation that a strict interpretation of the statute helps to ensure a more reasonable level of contributions is recovered from ratepayers.” (May 29, 2012 Order at 98) Staff asserts that these recent observations by the Commission support the conclusion that recoverable donations made for the public welfare should, at a minimum, be limited to Section 501(c)(3) charitable organizations. In addition, Staff states that the Commission has a long history of disallowing recovery for donations made to community and economic development organizations.

Staff takes issue with AIC's misrepresentation of Staff's position. AIC claims that reliance on Section 501(c)(3) would prohibit charitable contributions to local schools and governments. Staff avers that its recommendation does not do so and points out that its recommendation to use a Section 501(c)(3) filter only applies to donations made for the "public welfare." Because donations made for scientific, religious, or educational purposes are more easily recognized, no such filter would apply to those donations. Staff claims that AIC similarly misrepresents the holdings in Docket No. 11-0721.

Staff also identifies shortcomings in AIC's argument that the community and economic development organizations that Staff seeks to disallow are Section 501(c)(6) tax exempt organizations that receive donations. Staff considers it important to note that Section 501(c)(3) organizations are restricted in how much political and legislative lobbying activities they may conduct. A Section 501(c)(6) organization may further its exempt purposes by lobbying as its sole activity without jeopardizing its exempt status. Therefore, the tax exempt status of Section 501(c)(6) organizations is different than those of Section 501(c)(3). Furthermore, Staff states, there is no basis in the record to assume that the 501(c)(6) community and economic development organizations conduct themselves under the restrictions of the Section 501(c)(3) organizations.

With regard to AIC's IHSA donation, Staff acknowledges that the organization is a 501(c)(3) organization. Staff, however, is not viewing the contribution as a donation for the public welfare. Given the nature of the IHSA, Staff is considering the contribution under the "educational" category of Section 9-227 of the Act. Because the purpose of the donation was not for an educational purpose, as is required by Section 9-227, but rather in support of the state football playoffs, Staff recommends that the donation be disallowed.

b. AIC Position

AIC maintains that because the Commission rejected a similar Staff adjustment disallowing donations to economic development organizations in Docket No. 11-0721, the Commission should do so again here. According to AIC, the Commission found in that docket that the "term 'public welfare' only means contributing to the general good of the public." (May 29, 2012 Order at 98) The Commission stated further that "many organizations, including those . . . that promote community and economic development, contribute to the general good of the public." (*Id*.)

AIC disputes Staff's characterization of the Commission having previously disallowed donations to economic development organizations. Staff suggests that prior Commission decisions, including AIC's last completed electric rate case, Docket Nos. 09-0306, et al. (Cons.), support the exclusion of community and economic development donations in this case. AIC cites the Commission's recent findings in Docket No. 11-0721 as evidence of the Commission coming to conclusions contrary to the outcome in Docket Nos. 09-0306 et al. (Cons.). AIC states that the Commission found in Docket No. 11-0721 donations to be recoverable under Section 9-227's "public welfare" prong, if they "contribute to the general good of the public." (May 29, 2012 Order at 98) If any prior Commission decision should be considered controlling in this instance, AIC contends that it should be the decision just issued and directly on point.

As for Staff's claims concerning Section 501(c)(3) of the IRC, AIC maintains that the federal tax code is not the standard for determining what contributions to include in rates under Illinois law. AIC insists that Section 9-227 of the Act is the standard and does not limit cost recovery for donations based on the recipient's tax-exempt status. Nor, AIC continues, is it reasonable to graft such a limitation onto the statute. AIC states that Section 501(c)(3) organizations, although they represent a large portion of the organizations to which AIC makes donations, are not the only groups that receive donations. Non-profit local community and economic development organizations, which are tax exempt under another section of the IRC (Section 501(c)(6)), also receive donations from AIC. AIC adds that public schools and local governments, which do not qualify for tax-exempt status under Section 501(c)(3), receive donations as well. AIC laments that Staff's narrow reading of "charitable" would presumably prohibit the recovery of donations to local schools and governments that do not qualify for this particular tax exemption. AIC argues that simply because the IRS considers organizations described in Section 501(c)(3) to be those that are commonly referred to as "charitable" does not mean that Illinois must or should consider Section 501(c)(3) organizations as the only organizations that can receive recoverable donations under Section 9-227.

Even if it is reasonable to use the federal tax code to define "charitable" under Section 9-227, AIC points out that doing so would still not limit recovery under the statute’s “public welfare” prong. AIC argues that the Commission has found that donations are recoverable under the “public welfare” prong if they “contribute to the general good of the public,” and that community and economic development organizations “contribute to the general good of the public.” AIC asserts that Staff’s interpretation of what donations may be recoverable under the “charitable” prong does not change the basis for the Commission’s decision in ComEd’s formula rate proceeding. AIC insists that donations to non-profits whose mission is to nurture the development of local communities, attract new industry and jobs, expand existing businesses, or promote local tourism in the AIC service territory are made “for the public welfare” and should be a recoverable operating expense.

AIC denies having a policy of only seeking recovery of donations made to Section 501(c)(3) organizations. AIC asserts that Mr. Ogden made clear in his surrebuttal testimony that whether an organization is tax-exempt under Section 501(c)(3) is a factor AIC considers, but it is not the only factor that AIC considers when seeking cost recovery for donations pursuant to Section 9-227. (See AIC Ex. 26.0(Rev.) at 5-6)

c. Commission Conclusion

At issue here is not whether AIC may make donations to any organizations. AIC is free to make donations to any organization it chooses. At issue is whether or not ratepayers should reimburse AIC for the donations it chooses to make. Section 9-227 of the Act addresses when such expenses are recoverable from ratepayers. Staff recommends disallowing $72,000 that it believes is ineligible under Section 9-227 for recovery from ratepayers. AIC disagrees with these Staff adjustments.

The Commission has addressed this issue in prior rate orders. As noted above, the Commission recently initiated Docket No. 12-0457 to develop the rules on this issue that it deemed necessary after examining the issue in ComEd's first formula rate docket. Those rules are far from completion and the Commission must address this issue as part of resolving this docket.

Section 9-227 recognizes four categories of recoverable donations. The Commission agrees with Staff that it is generally understood what is meant by "scientific," "religious," and "educational." The Commission attempted to clarify in Docket No. 11-0721 what is meant by the fourth "public welfare" category when it described "public welfare" as "contributing to the general good of the public." (May 29, 2012 Order at 98) In doing so, the Commission also stated,

> The Commission agrees with CUB/City’s observation that a strict interpretation of the statute helps to ensure a more reasonable level of contributions is recovered from ratepayers. However, at this time, Staff and CUB/City have not given details as to how their recommendations would ensure that ratepayer funds are donated to charities that adequately serve ratepayers. (*Id*.)

Staff appears to have taken the Commission's concerns over the lack of details seriously and now advances an argument based on Section 501(c)(3) of the Internal Revenue Code. However, reliance on Section 501(c)(3), as Staff recommends, does not provide the intended clarity as to when a donation made for the "public welfare" would be recoverable from ratepayers. For instance, as a 501(c)(3) organization may also engage in limited political and legislative lobbying activities, there simply is not the bright line between 501(c)(3) organizations and 501(c)(6) organizations that Staff posits exists. While the Commission shares Staff's concerns about the nature of the activities that a 501(c)(6) organization (or, for that matter, a 501(c)(3) organization) could undertake, in this case the Commission takes at face value the descriptions of the funded activities as detailed in Ameren Exhibit 16.1, as accompanied by sworn testimony, and accepts that the contributions were made for the stated public welfare or scientific, educational, or religious purposes.

The Commission appreciates the difficulty in resolving this matter while the rulemaking in Docket No. 12-0457 is underway and the potential for differing standards to be applied over time. The Commission commends Ameren for providing more easily discoverable and reviewable information regarding the nature and purpose of the contributions than has been seen in some previous proceedings. This additional information has aided the Commission in reviewing the purpose of the donations and the reasonableness of their amounts, which is the Commission's duty under Section 9-227. However, the Commission is concerned about how some contributions have been categorized into one of the four purposes listed in Section 9-227 (public welfare, scientific, religious, and educational). For example, it is not clear why the contribution to the Illinois High School Association is listed as both public welfare and educational, while contributions to other high school athletic-related activities are just listed as educational. In the future, any additional information and explanation that a utility can offer will be useful to the Commission. That being noted, the Commission does not mean to suggest that the outcome of this decision must necessarily be followed in Docket No. 12-0457. The outcome of that rulemaking proceeding will be based on the record therein.

Having reviewed the contributions made by AIC, the Commission declines to adopt Staff's recommended disallowances with one exception: the Commission finds that AIC's donation to the City of Springfield is unreasonable for recovery from electric ratepayers because Springfield is not within AIC's electric service territory. As the City of Springfield is a municipal utility for electricity, donations made to that municipality do not aid the public welfare (insofar as the "public" is defined as being consistent with the universe of those Ameren serves, as the Commission believes it must) or otherwise benefit AIC electric customers.

2. Account 909

Within the USOA followed by electric utilities subject to Commission jurisdiction is Account 909 - Informational and Instructional Advertising Expenses. The USOA description of expenses recorded in Account 909 reads as follows:

> This account shall include the cost of labor, materials used and expenses incurred in activities which primarily convey information as to what the utility urges or suggests customers should do in utilizing electric service to protect health and safety, to encourage environmental protection, to utilize their electric equipment safely and economically, or to conserve electric energy.

Staff, AG/AARP, and CUB recommend various disallowances of electric related expenses recorded in Account 909. AIC contends that none of the adjustments are warranted.

a. Staff Position

i. Brand Related Expenses

Following the reorganization of AmerenCIPS, AmerenCILCO, and AmerenIP into AIC in 2010, AIC incurred expenses associated with an evaluation of its customers' ability to recognize its new name and logo. The costs in question funded, among others things, the use of focus groups and surveys conducted by an outside expert to identify issues with name recognition and name confusion. The end result was a revamping of AIC's post-merger consumer education materials and message that included a new "value statement." Staff proposes to disallow the electric portion of the brand-related expenses ($430,576) because they were not incurred for any of the allowable purposes described in Section 9-225 of the Act. Staff references AIC witness Ogden's testimony where he stated, "This particular communications effort in 2010 funded, among other things, the use and analysis of focus groups to clearly identify our customers' recognition of our name." (AIC Ex. 16.0 at 22) Staff contends that name recognition and market intelligence gathering do not benefit ratepayers in any way and are not an allowable advertising expense. In response to AIC's claim that the branding expenses were incurred to help customers better understand that the merger of the legacy utilities would not impact the performance, reliability, or safety of their service (See AIC Initial Brief at 49), Staff points out that if the costs of these name recognition studies are passed on to customers, then the amount that the customers are paying for electric service will be adversely impacted by the merger by increasing the rates charged to customers. Staff states further that the Commission has previously disallowed these types of brand-related expenses and urges the Commission to remain consistent with this policy.

ii. e-store Costs

Staff recommends the disallowance of $94,633 associated with the operation of an on-line store where employees can purchase branded clothing and items such as flashlights, coffee mugs, and hats. In support of its position, Staff points to the testimony of AIC witness Ogden, "these costs ($95,000) were incurred to purchase inventory for the online employee e-store. Much of the cost for the e-store related to this invoice was for stocking of AIC merchandise after the merger of the legacy utilities." (AIC Ex. 26.0R at 17) While AIC claims that these costs benefit employee morale and facilitate public recognition of employees as representatives of AIC, Staff argues that the costs associated with stocking an on-line store with corporate branded products are not necessary for the provision of safe, reliable utility service. Staff insists that these costs do not represent informational and instructional advertising but rather institutional or goodwill advertising and should be disallowed.

iii. Signage Costs

Following the merger of the three Illinois legacy utilities, AIC incurred expenses associated with a new sign in its Peoria headquarters lobby and vehicular magnets with the new company name. Staff proposes to disallow the electric portion of such costs, $599 and $3,406 respectively, on the grounds that the signage represents goodwill or promotional advertising. Staff also appears to recommend disallowing $1,200 associated with updating billboards at a sports park in East Peoria with the new AIC name and logo. Staff notes that Section 9-225(2) of the Act expressly states that advertising costs of a goodwill or institutional nature shall not be considered for the purpose of determining rates:

> In any general rate increase requested by any gas or electric utility company under the provisions of this Act, the Commission shall not consider, for the purpose of determining any rate, charge or classification of costs, any direct or indirect expenditures for promotional, political, institutional or goodwill advertising, unless the Commission finds the advertising to be in the best interest of the Consumer or authorized as provided pursuant to subsection 3 of this Section.

Staff recognizes that AIC considers the costs necessary to correctly identify AIC as the new provider of electric service in the service areas of the former legacy utilities. But in response to AIC's argument that the Commission should not condone the use of obsolete and dated signage, Staff observes that it was Ameren's decision to merge the legacy utilities that caused the signage to become dated. Staff maintains that the signage contains no allowable advertising delineated in Section 9-225 of the Act and represents a duplicative expense resulting from Ameren's decision to merge its legacy utilities. (The expenses are duplicative in the sense that ratepayers already paid for the signs that AIC replaced and now seeks recovery for.) Staff contends that AIC's customers should not be burdened with these expenses.

iv. Other Account 909 Expenses

Staff proposes to disallow $849,107 in advertising costs because it does not believe that AIC has provided sufficient justification for their inclusion in rates under Section 9-225. Staff acknowledges that AIC provided information in support of its advertising costs in response to Staff DR ST 2.07. Staff states that the information provided in the original DR response did not reconcile with AIC's FERC Form 1 Account

909 amount for two reasons. First, AIC's response to Staff DR ST 2.07 provided amounts and supporting invoices for the total company with no indication as to the allocation to the electric operations. Second, not all of the costs associated with Account 909 were included in AIC's response to Staff DR ST 2.07.

After Staff filed direct testimony adjusting advertising expenses to the amount supported by AIC, AIC provided a supplemental DR response, ST 2.07R (AIC Ex. 26.1), which included a 60% allocation factor applied to all of the costs to represent the electric jurisdictional amount of those costs. Staff also observes that AIC's DR response ST 2.07R included the rest of the costs included in Account 909 to reconcile to the amounts on FERC Form 1. Staff laments that the additional costs contained in the response to Staff DR ST 2.07R could not be verified. AIC provided additional invoices in response to Staff DR ST 6.04 (AIC Ex. 26.2), but Staff claims that it was not possible to verify the individual costs shown in ST 2.07R with the invoices provided in ST 6.04. AIC's perspective that a full-scale audit of advertising expenses is not necessary speaks volumes in Staff's opinion. Staff also claims that AIC misrepresents Staff's position that Section 9-226 requires a reconciliation of costs to invoice. Staff denies making such a claim and states that it instead applied the criteria of allowable advertising costs under Section 9-225 to determine if AIC's costs are just and reasonable. Staff avers that it is clearly unreasonable to include in rates historical costs which AIC cannot reconcile to an invoice. Because the burden of proof to show that these costs should be included in rates lies with AIC and AIC has not met that burden to recover these additional costs, Staff contends that the unsupported costs should be disallowed.

b. AG/AARP Position

i. Brand Related Expenses

AG/AARP point out that Section 9-225(3) of the Act sets forth the categories of advertising that shall be considered allowable operating expenses for an electric utility. Under Section 9-225(3)(i), political, promotional, institutional, and goodwill advertising are specifically excluded. Section 9-225(1)(d) defines "goodwill or institutional advertising" as being "designed primarily to bring the utility's name before the general public in such a way as to improve the image of the utility . . ." Upon consideration of these provisions, AG/AARP witness Brosch identified $718,000 of such goodwill expenses which AIC incurred to examine the "Ameren" name and corporate logo, including work done by a contractor to transition to the "Ameren Illinois" name within the Community and Public Relations functions. AG/AARP argue that these expenses are not reasonable or necessary for the provision of utility services and should be excluded in setting rates. They contend that the record is clear that the primary and prevailing purpose of these expenses were promotional and intended to advance the goodwill image of the utility, rather than to promote any allowable goal under the law. AG/AARP insist that AIC has failed to meet its evidentiary burden to properly isolate any portion of these branding related expenses that could be categorized as an allowable advertising expense.

AG/AARP note that AIC witness Ogden acknowledges that AIC customers have no choice for delivery services. (Tr. at 150) Yet he continues to argue that these branding expenses should be charged to its monopoly delivery service customers, based on the claim that in 2010 the merger and consolidation of the three legacy utilities created name confusion that made such expenses necessary to ensure that the public had accurate information so as to enable them to properly identify and/or contact AIC. (AIC Ex. 16.0 at 21) AG/AARP observe that AIC had already expended money to prominently place its new name and logo on the monthly bills that are sent to consumers; AIC workers in the field carry employee IDs that properly identify them as working for AIC; if a customer used a phone number from an earlier legacy company to make a call regarding a downed wire or other safety problem, that customer would still properly reach AIC because all previous phone numbers worked correctly; call center automated attendants already immediately advise consumers who call that they have reached AIC; and the utility's website is currently and prominently captioned with the AIC name and logo. (See generally Tr. at 149-152) Therefore, AG/AARP maintain that the additional funds at issue which were expended to explore customer reactions to a new corporate brand were not necessary to address customer confusion for public safety related purposes; rather those expenses were merely designed to promote AIC's goodwill image and new brand.

Furthermore, AG/AARP relate that Mr. Ogden testifies that such branding expenses will continue into the future. Specifically, Mr. Ogden states, "So it is a very dynamic element when you talk about customer research. So we do intend to continue to do that in helping us understand what messages do we need to deliver to customers and get the Ameren Illinois name recognized." (Tr. at 159) AG/AARP contend that such ongoing research is not plausibly related to the one-time merger and consolidation transitioning, and is not essential or necessary to the provision of electric delivery service.

AG/AARP also report that a significant portion of these contested 2010 branding expenses were paid to marketing consultants to conduct and analyze focus groups, and to develop Ameren's new value statement. AG/AARP assert that these are the type of expenses that the Commission has disallowed in a prior Northern Illinois Gas Company ("Nicor") rate case, stating, "The Commission is not persuaded that market intelligence gathering and other branding expenditures benefit ratepayers in any way. Such expenses therefore should not be borne by ratepayers." (Docket No. 04-0779, September 20, 2005 Order at 37) AG/AARP contend that AIC's new value statement ("Focused Energy. For Life."), is an obvious attempt at goodwill advertising and brand name puffery. They maintain that it is simply not believable that this vague slogan was intended as a message essential to public safety or to combating customer post-merger confusion over the identity of the electric company. When asked on the witness stand to give examples of the customer confusion that was being addressed, they note that Mr. Ogden first discussed confusion between the Missouri and Illinois media markets (Tr. at 153), but he later acknowledged that "Focused Energy. For Life." is a statement used by Ameren affiliates on both sides of the Mississippi River. (Tr. at 157) AG/AARP state further that Mr. Ogden acknowledged that some of the claimed expenses in this category do not relate to safety, storm preparation, electric supply choice, energy efficiency, or any other allowable category, claiming that “identity” was one of the goals of the expenditures in dispute. (Tr. at 161) Mr. Ogden, they observe, did not identify what portions were for corporate identity, as opposed to the other claimed categories. Because they believe AIC has failed to meet its evidentiary burden to properly isolate any portion of these branding related expenses that could be categorized as an allowable advertising expense, AG/AARP urge the Commission to adopt their proposed adjustment.

ii. e-store Costs

AG/AARP witness Brosch identified $158,000 of claimed expenses related to re-stocking an internal AIC e-store. Consistent with its legal analysis and discussion regarding AIC's branding expenses, AG/AARP believe that the expense for stocking the e-store with corporate branded merchandise is “institutional or goodwill advertising” that should not be borne by ratepayers. They argue that these expenses are neither reasonable nor necessary to the provision of utility services and thus should be excluded in setting rates. Moreover, AG/AARP observe that Mr. Ogden presumed that the re-stocking in 2010 was related to the adoption and transition to a new corporate name (Tr. at 163), and thus was likely to be higher than an ongoing, reasonable re-stocking expense might be going forward. Accordingly, AG/AARP recommend that the Commission disallow such e-store expenses in AIC's electric rates.

iii. Other Account 909 Expenses

AG/AARP argue that AIC has failed to meet its burden of proof to show that the amounts in dispute in this catch-all category concerning Account 909 are allowable expenses that consumers should bear. They observe that AIC failed to reconcile each vendor invoice with an appropriate subject matter. They also note that in its Initial Brief, AIC acknowledges that it has failed to perform this reconciliation, but argues that Section 9-226 does not require it. According to AIC, the new formula ratemaking law requires the utility to provide to the Commission the amounts spent on advertising and copies of all advertisements. AG/AARP reply that what the law does not say is that providing this basic information suffices to prove that such expenses are allowable advertisement expenses. AIC still bears the fundamental burden under the law to prove which, if any, of these expenses is allowable under the permissible types of advertising expense listed in Section 9-225 and that such expenses are reasonable and necessary for the provision of utility services. AG/AARP insist that AIC has failed to meet its burden, and thus the Commission should disallow these expenses.

c. CUB Position

i. Brand Related Expenses

CUB views corporate name-changing and related “branding” expense as similar to institutional advertising and corporate image building. CUB therefore contends that ratepayers of a monopoly utility should not be required to pay for such costs. CUB understands AIC to claim that its branding expenditures in 2010 were "necessary" following the consolidation of the legacy companies and AIC's name change. Specifically, CUB understands AIC witness Ogden to claim that AIC's expenditures on various marketing efforts, including paying a marketing firm to conduct focus groups and invent a new value statement, "Focused Energy. For Life.", were needed due to customer and media confusion about Ameren's subsidiaries. Mr. Ogden asserted that "identity efforts to get that identity of the Company emblazoned in [Ameren's] customer's minds" were of use when, for example, a customer needed to look up the phone number to call about a downed wire. (Tr. at 149) CUB observes, however, that Mr. Ogden also admitted that the phone number did not change when the AIC merger occurred. (*Id.*) CUB notes as well that AIC included in this expense "all efforts and items with Ameren Illinois logo and/or company name." (CUB Ex. 1.3 at 27, AIC Response to Staff DR ST 2.07) As further support for its proposed disallowance, CUB reminds the Commission that in Docket No. 04-0779, the Commission found that "market intelligence gathering and other branding expenditures" do not benefit ratepayers in any way. (September 20, 2005 Order at 36-37) Because AIC has not demonstrated that its branding costs are anything but promotional and corporate image-building in nature, CUB urges the Commission to disallow $403,000 in such expenses.

ii. e-store Costs

While AIC enables employees to purchase from its e-store company branded products for their own use, CUB suggests that AIC has failed to account for the revenues from such sales. Based on the cross-examination of AIC witness Ogden, CUB states that it is possible that revenues from the e-store are not reflected anywhere in the revenue requirement. CUB also understands that many e-store items are purchased by AIC departments and given to employees in recognition of exceptional safety records and performance or for community events. CUB observes that under cross-examination Mr. Ogden could only guess as to how those sales were expensed to various departments and did not know whether those expenses were recovered elsewhere, such as through a perquisites and awards expense. (Tr. at 168) CUB states that it is entirely possible that AIC is seeking double-recovery for e-store expenses, given that its witness did not know whether the amounts paid by employees for merchandise were used as revenues to offset the expense, or how internal AIC department purchases were recorded. Because CUB does not believe that AIC has not met its burden to demonstrate that this expense meets the requirements of Section 9-225, CUB urges the Commission to disallow the expense.

d. AIC Position

i. Brand Related Expenses

AIC maintains that its study of customers' perceptions of their service provider are recoverable expenses incurred in assessing the effectiveness of its customer education programs during the transition to a single operating company servicing one territory. AIC argues that this communications effort was not a public relations campaign to improve AIC's image, promote its services, or lobby in support of a controversial issue, but rather was a coordinated study to improve the effectiveness of its customer service to the benefit of ratepayers.

AIC indicates that the purpose of the branding study at issue was to address customer confusion over the identity of the service provider. AIC contends that customers have been confused over (1) which legacy utility provided electric and/or gas service, (2) whether AmerenUE was still an Illinois provider, and (3) which Ameren subsidiary was being discussed across the various overlapping local media markets. Following the consolidation of the legacy companies and the name change to "Ameren Illinois," AIC felt that it was necessary to address concerns with customer communications to ensure consumers had accurate information about their service provider and be able to properly identify their provider. AIC contends that this was not an effort that could be handled simply by the usual customer contacts (e.g., billings, signage, websites, and call centers). AIC claims that its branding study was an effort that was tailored to improve customer education services across the board.

AIC denies that the Commission decision in Docket No. 04-0779 is relevant here. In that decision, AIC states that the Commission had two concerns: (1) Nicor had not demonstrated adequate ratepayer benefit from the market intelligence gathering and other "branding" expenditures at issue; and (2) the branding expenses chiefly benefit the products and services of Nicor's unregulated companies. AIC insists that neither concern is present here. According to AIC, witnesses have only offered speculation that these "brand" related costs will benefit only unregulated Ameren affiliates.

AIC claims further that its branding expenses are in furtherance of the Commission's preference for uniform and best practices across the former legacy service territories. Specifically, AIC explains that the branding expenditures help it interact with customers in a consistent and clear manner. AIC characterizes the expenses as simply recoverable customer education expenses.

ii. e-store Costs

AIC contends that its e-store is in line with other large companies who make the sale of company products easier for their employees. This in turn, AIC continues, promotes employee morale and a sense of pride and ownership. Company use of e-store merchandise includes safety or other recognition awards. Branded clothing from the e-store is also worn by employees in the field or at AIC sponsored events so that customers or vendors may recognize them as representatives of AIC. Whether employees purchase the clothing or it is given to them by AIC for such purposes is not clear.

In response to Staff and certain intervenors' adjustments for e-store costs, AIC asserts that the purpose of restocking the e-store with AIC merchandise was not to improve AIC's image in the public or promote AIC's services to consumers, but to ensure that AIC branded merchandise would be available for personal purchase or AIC use. AIC insists that rewarding employees with AIC merchandise, using AIC merchandise for company events, and allowing AIC employees a medium for purchasing these products are justifiable operating practices. AIC recommends that disallowances concerning the e-store be rejected.

iii. Signage Costs

In 2010, at the time of the merger of the legacy utilities, AIC replaced signs, in part to reflect the new AIC name and logo, in other part to update billboards with new messaging. AIC understands that Staff is proposing to remove "signage" costs covering three items: (1) the replacement of a lobby sign to reflect the AIC name post-merger ($600); (2) the replacement of vehicle magnets to reflect the AIC name post-merger ($3,400); and (3) the replacement of AmerenCILCO artwork with Kids Act on Energy artwork on billboards at the East Side sports park in East Peoria ($1,200). AIC denies that these signage costs are "goodwill" or "promotional" advertising expenses not recoverable under Section 9-225 of the Act. These dollars, AIC argues, were spent to accurately identify it as the new service provider in the legacy territories or provide energy efficiency and safety messages to consumers. AIC explains that it did not replace its office lobby sign to improve its image; it replaced the sign to adhere to public notice requirements. AIC states further that it did not replace vehicle magnets to promote its services; it replaced the magnets so that its employees and contractors could properly be identified with the new provider. AIC adds that it did not erect billboard advertisements in East Peoria to promote a controversial message; it erected the billboards to provide messages to consumers about energy efficiency and safety. According to AIC, these are run-of-the-mill advertising expenses that should always be recoverable in rates.

That these expenses are recoverable is even clearer, AIC opines, when one considers the alternatives. The alternative to replacing the lobby sign and magnets to reflect the new AIC name would have been to continue to use the outdated lobby sign and vehicular magnets with the names and logos of the old providers. The alternative to erecting new billboard advertisements updating messages on energy efficiency and safety would have been to continue to use the old AmerenCILCO artwork. AIC claims that these alternatives would not have been prudent business decisions or of any benefit to its customers. AIC maintains that it makes no sense that a utility cannot recover the costs to replace signs that are necessary to properly identify the utility or that promote energy safety and efficiency. AIC states that the Commission should not condone the use of obsolete and dated signage and should reject Staff's signage adjustments. AIC states further that the absurdity of Staff's position is evident when Staff witness Tolsdorf testified that he would recommend disallowing expenses for replacing signs for wear and tear reasons. (See Tr. at 498)

iv. Other Account 909 Expenses

In any general rate increase proceeding, in which Section 9-225 of the Act applies, utilities are required by Section 9-226 of the Act to make available to the Commission copies of all advertisements and scripts included in the operating expense, listing the production costs for each ad, the publication schedule, and costs for each ad. (See also 83 Ill. Adm. Code 295.40(a)) AIC provided Staff with vendor invoices for advertising costs and a worksheet that detailed the various expenses that were charged to Account 909.

With regard to the brand related expenses, e-store costs, and signage costs, Staff identifies the specific expense it finds objectionable and why it is not recoverable. In total, those three disallowance areas would remove approximately $531,000 from AIC's electric formula rate revenue requirement. AIC observes that Staff's schedules disallow approximately another $849,000, without any explanation and without identifying the specific advertising expenses that were objectionable. AIC states that the reason for this apparent ambiguity is Staff's method of adjustment. Staff could have made specific disallowances to the total expense AIC charged to Account 909. Instead, AIC states that Staff builds an "allowable" amount of expense for Account 909 from the ground up that largely ignores the revised cost worksheet AIC provided (AIC Ex. 26.1) and the additional invoice support submitted. (AIC Exs. 26.2 and 26.3) AIC asserts that it presented Staff with a detailed breakdown by subject matter area of the electric expenses included in the FERC Form 1 data for this account, and with invoiced and non-invoiced amounts that support a substantial portion of the additional costs Staff seeks to exclude.

In response to Staff's suggestion that AIC failed to meet its burden under Section 9-226 because it did not reconcile each vendor invoice it provided with the subject matter expense listed in the detailed cost worksheet, AIC asserts that Section 9-226 requires no such showing. Section 9-226 requires AIC to identify the costs for each ad, which AIC claims it did in its response to Staff DR ST 2.07R. Section 9-226 also requires AIC to provide copies of the ads, which AIC claims to have done. At that point, Staff could have and did ask questions about particular expense items listed on Staff DR ST 2.07R. AIC acknowledges that it has not been able to show how each vendor invoice – some of which are total gas and electric costs – reconciles to the subject matter expense to the very last dollar, but contends that the Commission's review of advertising expenses should not be the equivalent of a full-scale IRS audit. Nor, AIC continues, should it be an exercise to see who can piece together the individual charges that make up the aggregate expense in any particular account. AIC believes that the documentation provided to Staff to detail the various advertising expenses charged to Account 909 and allocated to electric operations represents a reasonable effort – and certainly an effort that met AIC's burden under Section 9-226. Even if the Commission disallows costs for the three specific items Staff identified, AIC argues that Commission should not penalize AIC by making a further disallowance that is not tied to a particular objectionable advertisement.

e. Commission Conclusion

For purposes of resolving the issues concerning Account 909, the most relevant portions of Section 9-225 are arguably subsections (1)(c) and (1)(d). For ease of reference in discussing these issues, these subsections read as:

> (c) "Promotional advertising" means any advertising for the purpose of encouraging any person to select or use the service or additional service of a utility or the selection or installation of any appliance or equipment designed to use such utility's service; and
>
> (d) "Goodwill or institutional advertising" means any advertising either on a local or national basis designed primarily to bring the utility's name before the general public in such a way as to improve the image of the utility or to promote controversial issues for the utility or the industry.

i. Brand Related Expenses

Despite AIC's arguments to the contrary, the Commission is not convinced that AIC's brand related expenses are recoverable expenses. The types of activities that Staff and the intervenors describe are generally consistent with marketing efforts that fall under subsections (1)(c) and (1)(d) of Section 9-225. How, for example, having customers pay for the development of the phrase "Focused Energy. For Life.", which is used in both Missouri and Illinois, benefits customers as AIC contends is unclear to the Commission. Nor is it clear to the Commission why notice of the name change could not be handled through bill inserts, signage, websites, and call centers despite AIC's argument that such an effort could not be handled through such usual customer contacts. Moreover, the suggestion that such branding expenses are apt to continue in the future conflicts with AIC's assertion that the branding study was necessary in light of the legacy companies merger. For these and the reasons described by Staff and the intervenors, the Commission finds that AIC's brand related expenses should not be recovered from ratepayers.

According to AIC Ex. 26.1, the total costs associated with the study of the Ameren brand that was allocated to AIC is $717,626. That portion attributable to AIC's electric operations, or 60%, amounts to $430,576. Of this amount, 93.41% is allocable to AIC's delivery service (as opposed to transmission), which equals $402,201. Therefore, $402,201 shall be disallowed for AIC's brand related expenses.

ii. e-store Costs

The Commission has considered the parties' arguments concerning AIC's e-store expenditures. Although there is certainly nothing inappropriate about providing employees with a means to purchase company branded products, the Commission is troubled by AIC's premise that ratepayers should pay to stock the shelves. AIC's arguments do not persuade the Commission that the availability of such branded products for the purposes identified by AIC provide sufficient benefit to customers to warrant their payment of the expenses. Nor can there be any argument that the availability of branded products to employees is necessary for the provision of electric service. Rather, such branded products are more appropriately considered an element of goodwill advertising. For these and the other reasons set forth by Staff and the intervenors, the Commission concludes that an adjustment should be made disallowing AIC's e-store costs. Additionally, it is not clear how AIC accounts for sales from its e-store. Although this observation is independent of the decision on this issue, the Commission professes some concern over what may be double recovery for the same e-store expenses.

The adjustment for this disallowance is $88,397. This amount is calculated by multiplying the total AIC portion of the e-store costs from AIC Ex. 26.1 by 60% to determine the portion attributable to AIC's electric operations ($157,721 x 60% = $94,633). The resulting amount is then multiplied by 93.41% to determine the amount allocable to AIC's electric delivery service operations ($94,633 x 93.41% = $88,397).

iii. Signage Costs

Upon choosing to merge the legacy utilities, Ameren had at least three options regarding signage. One option would have been to retain the existing signage and only replace them when wear and tear warranted their replacement. At that point AIC could have sought recovery of its expenditures in rates. A second option would have been to replace the signage immediately following the merger and *not* include the expenses in rates. A third option, the one which AIC chose, would have been to replace the signage immediately following the merger and seek recovery of the expenses in rates. AIC chose the third option because it believes its signage expenses are reasonable expenses recoverable under Section 9-225 of the Act.

The Commission recognizes the importance of properly identifying company property and messages to the public. No party disputes that customers paid for the pre-merger lobby sign, vehicle magnets, and billboards through earlier rates. Nor does any party question whether such earlier expenditures and the recovery thereof were appropriate. But the Commission rejects the idea of making customers pay for such items again simply because Ameren chose to merge its three Illinois operating utilities.

The record is not clear as to what exactly the Peoria lobby sign looked like prior to the merger, but Staff witness Tolsdorf testifies that after the merger the lobby sign simply says "Ameren Illinois" next to the AIC logo. (Staff Ex. 15.0 at 9) With regard to the vehicle magnets, the record indicates that the only difference between the old magnets and new magnets is the company name. The only other information contained on the magnets is an e-mail address, which did not change after the merger. (*Id.* at 10-11) The paucity of the record on this issue is most apparent with regard to the East Peoria sports park billboards. AIC witness Ogden testifies that "the Kids Act on Energy 'signage' dollars provided valuable information to consumers about energy efficiency and safety." (AIC Ex. 26.0 at 14) Other than this description, the record contains no information as to what appeared on the billboards prior to the merger or after the merger. In future proceedings where such matters are disputed, the Commission strongly encourages the parties to offer for the record photographs of the signage at issue.

The Peoria lobby sign is probably the easiest to address. This sign contains only the company name and logo. The record also indicates that it was replaced simply because the company name changed. Why AIC would want a "current" sign hanging in its lobby is understandable, but how replacing this sign was beneficial to customers who had already paid for the prior sign is unclear to the Commission. As Mr. Tolsdorf pointed out on cross-examination, if someone is in the lobby of AIC's Peoria office, that person most likely knows where he is and a $600 sign will provide no further assurance. (Tr. at 496) Therefore, the Commission finds this expense duplicative and should not be recovered from ratepayers and instead should be born by shareholders.

The vehicle magnet signs are similar in that the only change appears to be the company name. As noted previously, this change only occurred because Ameren chose to merge its Illinois operating utilities. While having identifiable utility vehicles is important, the pre-merger vehicle magnets already identified the vehicles as belonging to Ameren, and ratepayers had already paid for those magnets. Again, the Commission cannot discern sufficient reason to justify having customers pay twice for essentially the same item. Because Ameren chose to change the name its Illinois operating utilities would be known by, its shareholders, and not ratepayers, should bear the associated costs.

As for the sports park billboards, because it is not clear what exactly is on the billboards, it is more difficult to determine if the associated costs are recoverable under Section 9-225. AIC contends that the post-merger billboards contain information about energy efficiency and safety. Expenditures for such categories of advertising are clearly recoverable under Section 9-225(3). But the pre-merger billboards could have contained the same information with only a different name and logo. If the new and old billboards contained essentially the same information, it is difficult to see why customers should cover the costs simply so the new company name and logo can be displayed. But if the new billboards advertised different information covered under Section 9-225, it is conceivable that customers should pay the costs. To resolve this issue, the Commission must rely on the fact that AIC bears the burden of proof. Under the totality of the circumstances concerning the signage expenditures and lack of sufficient information specifically relating to the sports park billboards, the Commission finds that AIC has not met its burden and that the $1,200 associated therewith should not be recovered from customers.

To be clear, these conclusions should not be construed to mean that the Commission would never approve recovery for replacement signage. Signage may experience wear and tear just like any other utility asset. Just like a wooden pole, if a particular sign is too worn or is otherwise damaged and is no longer useful, the Commission would expect AIC to replace that sign. In such instances, it is entirely possible that the Commission would approve recovery of associated expenses from customers.

iv. Other Account 909 Expenses

The Commission understands that Staff is recommending a general disallowance of expenses from Account 909 because it has not been able to tie specific invoices to particular advertising expenses that AIC seeks to recover from customers. Staff has not raised any specific objection to any particular advertising. The Commission understands Staff's concern and believes that the underlying problem for Staff is one of limited resources to devote to work that must be done under a shortened deadline. Regardless of the reason, the Commission is not comfortable accepting a general adjustment to a category of costs. In the absence of specific reasons behind objections to an expense, the Commission questions whether it can know if a disallowance is indeed warranted. AIC appears to have eventually provided the information called for in Section 9-226 and Staff's DRs. Given the lack of any detailed objections to any particular expenses, the Commission is not inclined to adopt Staff's adjustment. The Commission, however, does expect AIC to provide as much information as early as possible and as clearly as possible in the rate setting process.

3. Account 930.1 - General Advertising Expenses

For more general advertising expenses, the USOA contains Account 930.1 - General Advertising Expenses. The USOA description of expenses recorded in Account 930.1 reads as follows:

> This account shall include the cost of labor, materials used, and expenses incurred in advertising and related activities, the cost of which by their content and purpose are not provided for elsewhere.

Among general advertising expenses not provided for elsewhere are corporate sponsorship expenses. AIC provided several corporate sponsorships which it recorded in Account 930.1. Among the wide variety of organizations and events that AIC provided corporate sponsorships and now seeks to recover from ratepayers are local parades, festivals, plays, concerts, races, and the Illinois State Fair. Pages 15 and 16 of AIC Ex. 26.1 (see also Staff DR ST 2.07R) contain a list of events and organizations to which AIC provided funds. Staff, AG/AARP, and CUB recommend disallowing certain corporate sponsorship expenses which AIC believes are appropriate to include in its electric revenue requirement.

a. Staff Position

Staff reports that AIC provided financial support in the form of corporate sponsorships to several events and organizations in 2010. Staff contends that these sponsorships put AIC’s name in a good light in various communities and represent goodwill advertising which is prohibited by the Act from being recovered in rates.

Because the corporate sponsorships are primarily designed to improve the image of the utility or the industry, Staff believes that they are not appropriate for inclusion in Account 909. Instead, Staff contends that Account 930.1 is the proper account in which to record these types of expenses. But regardless of their account classification, Staff urges the Commission to deny recovery of such promotional and goodwill advertising represented in corporate sponsorships. Staff acknowledges AIC's claim that the "primary design of the corporate sponsorship is to financially support the worthwhile event itself" (AIC Initial Brief at 55), but points out that providing financial support to local festivals and events may represent good corporate citizenship but it does not meet the criteria in Section 9-225 for recoverable advertising expenses. The amount Staff recommends disallowing is $263,000, which is derived from AIC's response to Staff DR ST 2.07R.

b. AG/AARP Position

AG/AARP identify $236,000 of claimed expenses related to corporate sponsorships that they believe are not reasonable and necessary business expenses for the provision of utility service, and thus should be disallowed. AG/AARP observe that in its response to Staff DR ST 2.07, AIC identified a number of test year expenditures for tickets, signage, and sponsorship costs for various athletic events. They note that when AIC is recognized as a sponsor, it is the corporation brand that receives the appreciation, not its customers. AG/AARP recognize that corporate sponsorships can support good causes and help organizations and communities. They also state that AIC should be recognized for providing such help; customers, however, should not be compelled to underwrite such corporate sponsorships through electric distribution rates. They state that these expenses are not required to be incurred to provide public utility services and have been disallowed in the proposed adjustment. A copy of AIC’s confidential response to Staff DR ST 2.07 and its Attachment 1 are provided within AG/AARP Ex. 1.8. Moreover, consistent with their legal analysis and discussion relating to branding expenses in Account 909, AG/AARP believe that these sponsorships and related expenses constitute “institutional or goodwill advertising” and should not be recovered from electric delivery service customers.

c. CUB Position

CUB contends that AIC corporate sponsorship expenses amounting to $236,000 provide no benefits to ratepayers. These expenses include spending on basketball tournaments, game tickets, and holiday street decorations; none of which CUB avers is required for the provision of utility service, and none constitutes more than promotional, institutional, or goodwill advertising. According to CUB, AIC’s only justifications for these expenses are (1) that their sponsorships “work hand in hand with our employees’ volunteer activities,” and (2) that AIC “make[s] a difference in the well-being of our service territory and our customers." (AIC Ex. 16.0 at 25) CUB argues that those assertions do not satisfy the requirements of Section 9-225. While CUB finds AIC’s sponsorships admirable and states that AIC is free to continue sponsoring any events it chooses, CUB insists that AIC must use shareholder funds to do so and not be permitted to recover these expenditures from its customers.

d. AIC Position

In connection with its initial formula rate filing, AIC included an allocated electric portion of Account 930.1 expense in its revenue requirement and provided documentation concerning the advertising expenses charged to this account. AIC states that it has already excluded a substantial portion of Account 930.1 expense ($127,000) for costs incurred in sponsoring athletic events and purchasing sporting tickets. AIC rejects the notion that the remaining amount it seeks to recover from ratepayers ($263,000) for its corporate sponsorships should be disallowed as well.

AIC contends that the fact that it may receive public recognition in communities it serves by virtue of events it sponsors does not mean corporate sponsorship dollars are *per se* disallowable advertising. To disallow such advertising expenses, AIC argues, fails to consider that local events both rely on corporate sponsors and provide a benefit to communities. Moreover, AIC denies that its corporate sponsorships constitute “goodwill” or “institutional” advertising as set forth in Section 9-225 of the Act. AIC claims that it does not sponsor events to improve its image or promote controversial issues. Rather, AIC states that it sponsors these events because it believes these events are worthwhile and deserving of its financial backing. According to AIC, being a good corporate citizen is not about improving the utility’s name or promoting an issue the utility considers important; being a good corporate citizen is about supporting causes the public considers important. AIC does not believe that the legislature intended to exclude all corporate sponsorship expenses from rate recovery.

AIC notes that neither Staff nor the intervenors offer criticism of a specific corporate sponsorship. Even if it were tenable that corporate sponsorship of a particular event were “goodwill” or “institutional” advertising, AIC insists that the Act would still allow the cost to be recovered in rates if “the Commission finds the advertising to be in the best interest of the Consumer.” (Section 9-225(2)) While AG/AARP and CUB argue that these are discretionary expenses not required to provide utility service, AIC contends that this should not be the standard for a recoverable advertising expense. The standard, AIC argues, should be whether the advertising expense provides a benefit to the rate paying public.

In further support of its position, AIC asserts that no party opposing the recovery of corporate sponsorships has identified a prior Commission opinion that has disallowed these costs. For decades, AIC states that gas, electric, and water utilities have sponsored community events and recovered the related advertising expenses in rates. AIC maintains that this is not the occasion to disallow them.

e. Commission Conclusion

Section 9-225 of the Act is relevant to the expenses at issue in Account 930.1. Subsection (1)(d) appears to be the most relevant portion of Section 9-225 and is reproduced below:

> (d) "Goodwill or institutional advertising" means any advertising either on a local or national basis designed primarily to bring the utility's name before the general public in such a way as to improve the image of the utility or to promote controversial issues for the utility or the industry.

Section 9-225(2) prohibits direct or indirect expenditures for goodwill or institutional advertising from being included in rates unless found "to be in the best interest of the Consumer."

AIC Ex. 26.1 contains a list of AIC's 2010 corporate sponsorships, some of which AIC has already excluded from rates on its own. "Self-excluded" costs include those for athletic events and tickets. AIC claims that the remaining corporate sponsorships do not constitute goodwill or institutional advertising and are thus recoverable from ratepayers under Section 9-225. The fact that its name is brought before the public and its image may be improved as a result of the sponsorships is strictly incidental, according to AIC.

The Commission has considered the parties' arguments and observes that none deny that corporate sponsorships are important to the success of many organizations and events. Nor do any of the parties suggest that AIC is not free to engage in corporate sponsorships as it believes appropriate. But the value of the sponsorships to the recipients and AIC's choice of events to sponsor need not be determined by the Commission. Whether customers should have to reimburse AIC for its decision to sponsor an organization or event is what hangs in the balance. Clearly the sponsorships that AIC has withdrawn from consideration on its own are not recoverable under Section 9-225. The withdrawn sponsorships do not seem all that different from those for which AIC still seeks recovery; the main difference being that AIC did not physically receive tickets/admission to an event. But regardless of whether AIC received tangible benefits for its corporate sponsorships, the Commission cannot disregard the fact that the sponsorships bring AIC's name before the public in a philanthropic light. While AIC claims this is not its intention, this is the very meaning of goodwill advertising. AIC is free to be a good corporate citizen and enjoy the ensuing benefits, but it should not be free to pass the costs of doing so to customers. That the Commission may not have made similar adjustments in past rate cases does not bar the Commission from doing so now since the Commission's failure to do so now that this issue has been brought to its attention would contravene Section 9-225. Accordingly, the Commission accepts Staff's $263,000 adjustment disallowing the costs of corporate sponsorships. Because they have incorrectly calculated their proposed $236,000 adjustment, the AG/AARP and CUB adjustment value is not adopted.

4. Regulatory Asset Amortization

a. AG/AARP Position

Section 16-108.5(c)(4)(G) of the Act requires that a participating utility's formula rate shall provide for "recovery of existing regulatory assets over the periods previously authorized by the Commission." AIC Ex. 2.1 at page 8, Sch. FR C-1, line 18 includes $7.131 million of "Regulatory Asset Amortization" within the revenue requirement. AIC's 2010 test year regulatory asset amortization amount is comprised of $352,000 for severance cost amortization and $6,779,000 for integration cost amortization. According to AIC's responses to several AG data requests, the origin of these two regulatory assets can be traced to specific severance and merger-related actions.

AG/AARP report that a severance cost amount that was incurred and recorded in 2009 was allowed regulatory recovery via amortization in Docket Nos. 09-0306 et al. (Cons.). Amortization over three years was recorded starting in May of 2010 in the monthly amount of $43,999. Since only eight months of amortization was recorded in 2010, AIC has included a total of $352,000 in test year expense for this regulatory asset.

Regulatory asset recovery of merger integration costs commenced after Ameren acquired IP and received regulatory approval in Docket No. 04-0294 for this reorganization, and was granted corresponding amortization and recovery of a total of up to $67 million of merger integration costs over a four-year period from 2007 through 2010. In the subsequent Docket Nos. 09-0306 et al. (Cons.), the remaining balance for the integration cost regulatory asset was recalculated to be amortized over two years. AG/AARP relate that this produced an irregular pattern of monthly integration cost amortization expenses in 2010, with $1.015 million recorded in each of the first four months of the year and $0.34 million recorded monthly from May through December of 2010. AG/AARP Ex. 1.6, attached to Mr. Brosch's testimony, includes complete copies of the AIC responses to DRs AG 1.12, AG 4.05, AG 4.06, and AG 4.07 that address these regulatory asset amortization matters.

AG/AARP witness Brosch proposes an adjustment to amortization expense to conform with the amortization periods and amounts most recently approved by the Commission in Docket Nos. 09-0306 et al. (Cons.). In that earlier proceeding, AG/AARP relate that amortization over specified periods produced monthly expense amounts of $43,999 and $339,630 for the severance and merger integration regulatory assets, respectively. Aside from the requirements of the Act, AG/AARP contend that it is appropriate to restate the test year recorded amortization expenses to match the Commission-authorized recovery periods and amounts. AG/AARP assert that the AIC rates being set at this time will tend to under-recover severance costs and over-recover merger integration costs unless Mr. Brosch's proposed adjustment is made to restate recorded expenses to Commission-authorized amortization periods and annual expense levels. Using the rescheduled amortization periods ordered by the Commission in Docket Nos. 09-0306 et al. (Cons.) will also help to ensure that completion of amortization occurs on the books within a future reconciliation period, so that ratepayers receive proper reconciliation credit for such expiring amortizations, Mr. Brosch explains.

AG/AARP characterize AIC's response to their position as simply based on specious legal arguments. According to AG/AARP, AIC wants the Commission to ignore evidence that the recorded amounts are inaccurate and inconsistent with recent Commission findings that update these amortization amounts. They perceive AIC as applying a tortured reading of the words “periods” and “previously” in Section 16-108.5(c)(4)(G) to argue that the Commission should ignore its previous findings in its Order in Docket Nos. 09-0306 et al. (Cons.). But in AG/AARP's view, Section 16-108.5 in no way precludes ratemaking adjustments to restate amortization expenses at authorized annual levels of expense. In fact, they view the new statute as specifically retaining Commission authority to “initiate and conduct an investigation of the (formula rate) tariff in a manner consistent with the provisions of this subsection (c) and the provisions of Article IX of this Act to the extent they do not conflict with this subsection (c)." (Section 16-108.5(c))

AG/AARP Ex. 3.1 at page 4, line 1 shows the monthly amortization expense previously authorized by the Commission for 2009 severance costs (column c) and merger integration costs (column d). These amounts are multiplied by 12 at line 2 to derive the equivalent annual amounts last authorized by the Commission. When compared to AIC’s proposed annual expense levels (at line 4), the adjustments needed to conform amortization expense to the amortization periods previously authorized by the Commission appear at line 5 and line 6, with the total amount carried forward to AG/AARP Ex. 1.3, page 1 in column (e). AG/AARP urge the Commission to adopt these adjustments.

b. CUB Position

CUB supports the adjustment proposed by AG/AARP to modify the amortization of two regulatory assets. CUB views Section 16-108.5(c)(4)(G) as requiring a participating utility’s formula to provide for recovery of existing regulatory assets over the periods previously authorized by the Commission. CUB agrees that AG/AARP witness Brosch accurately adjusts amortization expense to conform with the amortization periods and amounts approved in Docket Nos. 09-0306 et al. (Cons.).

According to CUB, the arguments presented by AIC are based on a flawed reading of the Act. AIC witness Stafford argues that, despite the fact that the statute requires recovery of regulatory assets over the Commission previously-authorized periods, it in fact meant that amortization should be whatever was reported in the FERC Form 1. CUB maintains that AIC’s position requires a strained and narrow reading of the statute, including a convoluted evaluation of the significance of the plural of the word “period,” and giving new meaning to the word “previously.” CUB therefore supports an adjustment of $2.523 million for this expense.

c. AIC Position

AIC set its 2010 regulatory asset amortization amount using the periods previously authorized by the Commission. Therefore, it believes that these amortization amounts are properly included in the Rate MAP-P revenue requirement. AIC objects to AG/AARP witness Brosch's proposal to adjust the 2010 amortization expense to reflect the same monthly amount of amortization expense for these two items for all 12 months of 2010, as if the monthly amount of amortization that resulted from the 2009 rate case had been in effect throughout 2010. The resulting revenue requirement impact of this adjustment is a $2,523,000 reduction.

AIC also notes that in Docket Nos. 09-0306 et al. (Cons.), the Commission agreed to a proposed modification to the amortization period for merger integration costs and authorized AIC to begin amortizing severance costs. These changes took effect at the time of new rates in May 2010, and the monthly amortization amount changed. The change in actual monthly amortization amounts mid-2010 is reflected in the 2010 FERC Form 1. Mr. Brosch, in contrast, is requesting that the changes that began in May 2010 and were reflected in FERC Form 1 be ignored in the calculation of the revenue requirement.

The view that AG/AARP's adjustment is permitted under the statute is incorrect in AIC's opinion. Section 16-108.5(c)(4)(G) authorizes "recovery of existing regulatory assets over the periods previously authorized by the Commission," and so in AIC's opinion requires the use of actual amortization as reported on FERC Form 1 for the rate year, which in this case is the rate year 2010. Moreover, AIC continues, Mr. Brosch's proposal is a form of annualization [normalization]. AIC states that Section 16-108.5 does not require normalization of expenses. (See Section 16-108.5(d)(3))

While there are numerous sections of the Act that discuss establishment of the performance-based formula rate revenue requirement based on the most recent FERC Form 1 data, AIC states that there is no mention of annualized cost inputs to the formula. Furthermore, AIC contends that the statutory language Mr. Brosch cites at Section 16-108(c)(4), if read carefully, actually supports making no annualization adjustment. The language states: "recovery of existing regulatory assets over the periods previously authorized by the Commission." Noting that this language uses the word "periods" rather than "period," AIC argues that there would be no need for this word to be plural if the intent was to use "the more recent period" or "the current period" for amortization. In addition, AIC asserts that the intentional use of the word "previously" rather than, for example, use of the word "currently" also supports AIC's interpretation that if more than one amortization period existed in a year, then more than one should be applied in the calculation of the year's amortization amounts. Moreover, because formula rates will be reset annually, AIC maintains that there is no need for a pro forma or annualization adjustment, as proposed by Mr. Brosch. Rather, AIC states that formula rates are intended to be set based on actual expense. For these reasons, AIC recommends that the Commission approve its proposed regulatory asset amortization.

d. Staff Position

Staff disagrees with AG/AARP's proposed adjustment. Staff states that the proposal does not comport with Staff's understanding of Section 16-108.5 because the statute does not mention a restatement of actual expense as part of the recovery of regulatory assets over the periods authorized by the Commission. Staff notes that it is not necessary to normalize the amortization expense because the formula rates will be set each year, and the actual cost recovery of these amounts will not give rise to under- or over-recovery of these expenses. Moreover, Staff notes that Section 16-108.5(d)(3) indicates that "normalization adjustments shall not be required." Staff urges the Commission to reject AG/AARP's proposed adjustment to regulatory asset amortization expense.

e. Commission Conclusion

The Commission has considered the parties' arguments and reviewed the statutory language. Section 16-108.5(c)(4)(G) provides for the "recovery of existing regulatory assets over the periods previously authorized by the Commission." Previous to the enactment of Public Acts 97-0616 and 97-0646, in Docket Nos. 09-0306 et al. (Cons.) the Commission authorized revised amortization periods for AIC's severance costs and merger integration costs. The Commission recognizes that the monthly amortized expense for both regulatory assets changed in May of 2010 with the entry of the Order in Docket Nos. 09-0306 et al. (Cons.). The Commission also recognizes that AIC is basing its formula rate on the data and information contained in its 2010 FERC Form 1, which will reflect different numbers on a going-forward basis, at least as far as the amortization of AIC's regulatory assets is concerned.

A plain reading of the statute indicates that a participating utility is to recover however many regulatory assets it has over whatever period the Commission previously authorized for each asset. With multiple regulatory assets, there will be multiple "periods." When considered in the context of this proceeding, AIC's two regulatory assets are to be recovered over the period previously authorized for each in Docket Nos. 09-0306 et al. (Cons.). It is the understanding of this Commission that AIC's FERC Form 1 reflects the actual regulatory amortization expense for 2010, in accordance with the amounts and periods previously authorized by the Commission. Although AIC and Staff cited to irrelevant statutory language in Section 16-108.5(d)(3) which does not apply to a participating utility's initial formula rate docket, the Commission does not find Mr. Brosch's adjustment consistent with any provision of the Act and hereby rejects the adjustment.

VII. REVENUES

The only unresolved revenue issue pertains to late payment revenues. Late payment charges are added to ratepayers' bills when payments have not been received by bill due dates. Electric Service Schedule Ill. C.C No. 1, Original Sheet No. 3.018

provides for a ". . . late payment charge equal to 1.5% per month" to be assessed "on any amount considered past due," as more fully described in the tariff.

A. AG/AARP Position

In the 2010 test year, AIC recorded as "forfeited discounts" in Account 450 - Forfeited Discounts[3] total late payment revenues of $11.38 million, as shown at AIC Ex. 2.1, page 28 within App 10. Rather than accounting for all of these recorded revenues within its asserted revenue requirement, AG/AARP observe that AIC applies a "revenue" based allocation factor of 41.89% which results in only $4.767 million of the total recorded late payment revenues being recognized for ratemaking purposes. AIC uses 41.89% because this percentage of revenues from a customer's electric bill generates the late payment charges for electric delivery service. This diminished $4.767 million value is carried forward as part of the total $24.7 million of Other Operating Revenues from line 14 of App 10, for inclusion as a revenue credit to the overall revenue requirement at AIC Ex. 2.1, page 1 (Sch. FR A-1) at line 21. AG/AARP explain that AIC seeks to treat as non-jurisdictional for ratemaking purposes the other 58.11% of the late payment revenues. The result is that the balance of the late payment charge revenues is not being credited to reduce the revenue requirement and will be retained by shareholders, because no other regulatory jurisdiction would receive any revenue credits for this other 58.11% share. AIC provides additional arguments for shareholder retention of late payment charge revenues in its response to DR AG 4.14, which has been entered into the record as part of AG/AARP Ex. 1.5.

AG/AARP also observe that AIC has not attributed any of the late payment charge revenues to the FERC's jurisdiction. Wholesale transmission services are regulated by FERC and AIC submits annual formula rate adjustment applications with FERC to update its cost-based open access transmission rates based upon current costs and revenues. When allocations are aligned or conformed between the Commission and FERC jurisdictions, AG/AARP state that AIC will recover 100% of its costs overall after consideration is given to expenses, rate base investments, and revenue credits that are available to offset such costs. AIC, however, does not allocate any portion of its late payment revenues to the FERC jurisdiction for ratemaking purposes and does not provide service in any jurisdictions other than Illinois and the FERC. AG/AARP conclude that AIC's creative but specious rationale for denying ratepayers the benefit of these late payment revenues should be rejected.

AG/AARP point out that in Docket No. 10-0467, the Commission addressed the proper jurisdictional allocation of late payment revenues. In that case, AG/AARP relate that ComEd had proposed retaining a substantial share of its late payment revenues for its shareholders, through application of a revenue-based allocation factor, similar to AIC's proposed treatment of these revenues. In its May 24, 2011 Order, the Commission rejected ComEd's proposed allocation methodology and accepted the adjustment recommended by AG/CUB witness Brosch. (Order at 306)

[3] Pursuant to the USOA, Account 450 shall include the amount of discounts forfeited or additional charges imposed because of the failure of customers to pay their electric bills on or before a specified date.

As noted by AG/AARP witness Brosch in this proceeding, the situation with regard to AIC's late payment revenues is nearly identical to that of ComEd, except that AIC is not crediting any of its late payment charge revenues to the FERC jurisdiction for ratemaking purposes. Consistent with the Commission's conclusion in Docket No. 10-0467, AG/AARP assert that late payment revenue should be treated as 100% Commission-jurisdictional and not be subject to any arbitrarily applied revenue-based allocation factor that would allow AIC shareholders to retain a portion of such revenues. These amounts, AG/AARP aver, are paid entirely by retail ratepayers pursuant to Commission rules and AIC's tariff.

AG/AARP also find it significant that AIC's proposed treatment of late payment revenues is inconsistent with its treatment of other customer provided funds. As an example, they point out that customer deposits are assessed based upon the relative size of anticipated customer bills and such deposits serve to secure payment for all elements of billed revenues, including recovery of power supply, transmission, and distribution cost recoveries. At AIC Ex. 2.2, page 51 Workpaper 2, AG/AARP note that customer deposit balances are treated as 100% jurisdictional in determining delivery service revenue requirements. AG/AARP maintain that this is an appropriate treatment of these funds, and a similar 100% assignment to retail delivery services should also apply to late payment revenues. AG/AARP's adjustment to Other Revenues appearing in column (d) of AG/AARP Ex. 3.3 includes a reversal of AIC's proposed jurisdictional allocation of late payment revenues, and a more detailed calculation of the adjustment Mr. Brosch proposes is set forth at page 3 of AG/AARP Ex. 1.3.

In response to their proposal, AG/AARP state that AIC witness Stafford agrees with Mr. Brosch that the entire amount of late payment revenues are Commission jurisdictional, but does not agree that all such revenues should be attributed to electric delivery service. AG/AARP understand Mr. Stafford to support attribution of some unspecified amount of late payment revenues to Rider PER – Purchased Electricity Recovery. They observe that he also makes multiple references to various non-delivery service tariffs and riders in relation to his claim that the unbundling of electric delivery service does not support AIC recovery of all costs through electric delivery service rates or apply all revenue credits to electric delivery service revenues. (See AIC Ex. 13.0 at 28-29) According to AG/AARP, AIC fails to demonstrate that these other charges to consumers have actually been reduced to account for any crediting of late payment revenues. Instead of making this showing, AG/AARP state that Mr. Stafford suggests that some alleged but unquantified under-recovery of power supply costs may result if AIC's shareholders are not allowed to retain more than half of late payments revenues. In response to these arguments, Mr. Brosch observed that AIC has made no showing that any relevant costs were not recovered or any facts that justify shareholder retention of such revenues.

AG/AARP find the notion that the unbundling of electric supply, transmission, and delivery service justifies AIC's proposed retention of the majority of late payment revenues for indirect recovery of otherwise under-recovered costs creative but not correct. In each rate case there should be a full and complete accounting for all AIC revenues, including late payment revenues. AG/AARP presume that AIC would have cited any past Commission decision specifically addressing jurisdictional allocation of late payment charge revenues if the issue had previously been considered and resolved as AIC proposes in this docket. Instead of providing such a specific citation to a relevant litigated issue, AG/AARP point out that Mr. Stafford simply references the Commission's past acceptance of AIC's allocation procedures. They reiterate that when the Commission specifically addressed the jurisdictional treatment of late payment charge revenues as proposed by Mr. Brosch for ComEd in the context of formula ratemaking, the Commission accepted that proposal.

Mr. Stafford's suggestion to address their concerns through later revisions to Rider PER does not satisfy AG/AARP. They note that until such revisions occur (assuming they do occur), AIC will retain late payment revenues for shareholders and overstate the delivery service revenue requirement. AG/AARP assert that, absent substantial evidence to the contrary, it is reasonable to assume that each of the various tariffs and riders mentioned by Mr. Stafford that are separately administered for AIC operations are properly based upon reasonable isolation of relevant costs for recovery through such tariff/riders. They state that AIC failed to provide such contrary evidence or quantify any alleged under-recoveries through other riders or AIC tariffs, particularly of any magnitude sufficient to justify shareholder retention of millions of late payment charge revenues each year. If there is some deficiency in cost recovery in a particular tariff or rider, or a "need to establish a separate tariff," AG/AARP contend that AIC or some other party should petition the Commission to remedy any cost recovery problems that exist. They insist that it is not reasonable for AIC to exclude late payment revenues from the delivery services jurisdiction because of some perceived but unproven under-recovery of Rider PER costs, or other costs AIC believes are not being reasonably recovered through some other rider or other rate element.

AG/AARP object to AIC's shifting to Mr. Brosch the burden of analyzing and adjusting for a myriad of imagined problems in other AIC rates and riders. Mr. Stafford claims that Mr. Brosch's "proposal to assign 100% of late payment revenues to electric DS service might have some merit if he had also proposed to include electric power supply costs in his calculation of CWC, rejected AIC's reduction to revenue requirement for removal of the electric power supply portion of uncollectibles, rejected application of the revenue allocator to ADIT related uncollectibles, and rejected AIC's reduction to A&G expense for production employee related pension and OPEB costs and electric power supply procurement costs." (AIC Ex. 13.0 at 29) But according to AG/AARP, if there are any supply related costs or adjustments that are necessary, one would expect those issues to be addressed in connection with the administration of Rider PER. Mr. Brosch adds that if AIC has a positive CWC requirement associated with its power supply function, AIC should be required to quantify this requirement and modify Rider PER. AG/AARP state that the effect of AIC's position would be to let shareholders retain millions of late payment revenue dollars just in case such a cost exists and is not being fully recovered. Similarly, if AIC showed that there are actual under-recoveries due to the rate of uncollectibles for supply charges, AG/AARP contend that a better response would be to request modification of Rider EUA - Electric Uncollectible Adjustment to revise uncollectible recoveries based upon relevant, actual factual data, rather than permitting shareholder retention of late payment revenues on the unproven premise that they could be compensatory for such alleged but unstated under-recoveries.

As for Mr. Stafford's claim that it would be necessary to reject AIC's reduction to A&G (administrative and general) expense for production employee related pension and OPEB costs and electric power supply procurement costs if late payment revenues are not partially retained for shareholders, AG/AARP assert that he has made no showing that the jurisdictional treatment of late payment revenues has anything to do with pension and OPEB cost adjustments otherwise made by the Commission. They note that he also lists a multitude of other tariffs and riders and states that Mr. Brosch should have included unspecified "rider related costs in revenue requirement" in connection with allocation of 100% of late payment revenues to delivery service rates. AG/AARP claim that this argument is plainly specious and that they are not obligated to perform cost of service studies or reconciliation audits for all of AIC's various rate riders in order to determine this utility's overall formula revenue requirement. In fact, when AIC developed the revenue-based allocation factor that it applied to late payment revenues, AG/AARP point out that AIC did none of these things that it now demands of them.

B. CUB Position

CUB supports the adjustment of AG/AARP witness Brosch with respect to AIC's late payment revenues. The "revenue" based allocation employed by AIC results in only 41.89% of the total recorded late payment revenues being recognized for ratemaking purposes. AIC does not allocate any portion of its late payment revenues to the FERC jurisdiction, which CUB states is the only other possible jurisdiction pertaining to this revenue. CUB therefore concludes that Ameren's shareholders retain 58.11% of late payment revenues. AIC's arguments with regard to Rider PER, i.e. that the Commission should allow Ameren to retain for shareholders the majority of late payment revenues at this time and then address changes to Rider PER at a later date, do not in CUB's opinion change the facts of this proceeding. Mr. Brosch testifies that any alleged problems that may exist with Rider PER are independent of this formula rate review, and in this docket, the Commission should correct the inappropriate allocation of late payment revenues. CUB also observes that the Commission addressed a similar issue in Docket No. 10-0467 concerning ComEd and adopted Mr. Brosch's position in that proceeding. CUB asserts that the same result is appropriate here.

C. AIC Position

AIC objects to AG/AARP witness Brosch's recommendation regarding late payment revenues for several reasons. First, AIC claims that the Commission's long-standing practice for AIC, in rate orders dating back at least to the unbundling of electric service rates in Docket Nos. 06-0070 et al. (Cons.), has been to include in the electric delivery service cost of service only electric distribution system costs recovered through electric delivery service base rates. AIC states that “other revenues” assigned or allocated to delivery service have been consistently used to offset the delivery service revenue requirement. AIC states further that revenues and costs associated with functions other than delivery service, such as power supply and transmission, are accounted for through separate tariffs submitted to, approved by, and subject to, this Commission’s jurisdiction.

Mr. Brosch contends that because none of the late payment revenues are allocated to FERC accounts, all of these revenues must be credited to delivery service customers. But just because a component of costs is billed to delivery service customers does not, according to AIC, mean that it should recover all costs and revenues through electric delivery service rates. To do so, AIC contends, would beg the question of why it was necessary to establish separate tariffs and riders for power supply, transmission service, and numerous other functions and services. AIC maintains that Mr. Brosch’s adjustment would effectively re-bundle electric service (at least for ratemaking purposes) by disregarding these separate tariffs and riders and their associated revenues and costs.

AIC's second reason for opposing the AG/AARP adjustment is that it is asymmetrical. Mr. Stafford testifies that Mr. Brosch’s proposal to assign 100% of late payment revenues to electric delivery service might have some merit if he had also proposed to include electric power supply costs in his calculation of CWC, rejected AIC's reduction to revenue requirement for removal of the electric power supply portion of uncollectibles, rejected application of the revenue allocator to ADIT-related uncollectibles, and rejected AIC's reduction to A&G expense for production employee related pension and OPEB costs and electric power supply procurement costs. Mr. Brosch did none of these things. According to AIC, reducing revenue requirement for power supply costs but at the same time including all power supply-related late payment revenues as an offset to electric delivery service revenue requirements is asymmetrical and unfair.

Third, AIC denies that the AG/AARP adjustment is consistent with the Commission’s treatment of late payment revenues in Docket No. 10-0467. AIC argues that the evidence in that case showed that ComEd characterized as non-jurisdictional approximately $16 million in late payment revenue from its delivery services revenue requirement, but only $2 million of this amount was allocated to FERC jurisdictional accounts. (See May 24, 2011 Order at 303-04) Under ComEd’s tariff, AIC states further, ComEd charged (and received) late payment revenues on the entire outstanding balance of bills, including supply and transmission charges. AIC also observes that the Commission noted, “all parties seem to agree that ComEd actually received these late payments charges, and, that it receives a profit upon both delivery services and the actual electricity it procured, in the form of these late payment charges.” (*Id.* at 305) Given these circumstances, AIC understands the Commission to have concluded that all but the $2 million in FERC jurisdictional late payment revenues was allocable to delivery service customers. AIC maintains that the Commission’s decision did not hinge on how much in late payment revenues were allocated to FERC. Rather, AIC reports that the Commission stated "ComEd was not able to identify how the remaining $13.9 million is credited to consumers or otherwise accounted for." (*Id.* at 303) AIC contends that here the evidence shows that approximately 42% of late payment revenues are attributable to distribution service costs recovered in base rates. The remaining revenues, AIC explains, are attributable to costs recovered through other tariffs and riders. To the extent the Commission is inclined to re-examine Rider PER, which recovers most electric supply costs, to more precisely track power supply costs and revenues, AIC urges it to do so in the context of the rate redesign proceeding to be initiated under Section 16-108.5(e), or at the time of the next Rider PER update filing.

D. Staff Position

Staff opposes AG/AARP's adjustment to allocate 100% of late payment revenues as an offset in the determination of rates in this proceeding. Staff agrees with AIC that the adjustment would run counter to the Commission's long-standing practice to include in electric delivery service revenue requirements only electric distribution system costs. Staff also agrees with AIC that Rider PER may need modifications regarding these revenues.

Staff notes AIC's comment that past Commission treatment of customer deposits as a 100% deduction to rate base should possibly be changed to align with the treatment of late payment revenues. Staff observes further that AIC is not opposed to the present treatment, or that application of a revenue allocator to customer deposits would be appropriate if Rider PER were modified. Since AIC's proposed treatment to deduct 100% of customer deposits is consistent with past delivery services orders, and no party appears to object to such treatment, Staff does not propose any adjustments either, and notes that this issue may need to be revisited in the future depending on any revisions made to Rider PER.

E. Commission Conclusion

The Commission has considered the parties' positions on this issue and finds in favor of AG/AARP. As AG/AARP argue, it does not seem proper that less than 42% of late payment revenues are used to offset AIC's revenue requirement. Late payments and the late fees imposed thereon are attributable to a customer's entire bill. To apply only the proportion of ratepayer supplied funds in Account 450 equal to electric delivery service and ignoring the remainder represents a windfall to shareholders.

The Commission recognizes that electric delivery service revenue requirements typically only include costs associated therewith. But at the same time, other sources of income/revenue have not been tied or limited to the proportion of revenue derived from delivery services alone. As AG/AARP note, customer deposits are assessed based upon the relative size of anticipated customer bills and such deposits serve to secure payment for all elements of billed revenues, including recovery of power supply, transmission, and distribution cost recoveries. Customer deposit balances are treated as 100% jurisdictional in determining delivery service revenue requirements. State and local taxes are treated similarly, and any assessed late fees are imposed on the tax portion of a bill as well.

In order to prevent an under recovery in certain areas, AIC suggests that other adjustments may be necessary if AG/AARP's proposal is adopted. AIC recommends denying AG/AARP's recommendation and reconsidering it and other appropriate adjustments, including adjustments to Rider PER, in the context of a future rate redesign proceeding to be initiated under Section 16-108.5(e) or at the time of the next Rider PER update filing. In the absence of compelling evidence that such other adjustments are necessary; however, the Commission is not inclined to wait to address this shortcoming in the adjustments to AIC's revenue requirement. Retaining for shareholders 58% of late payment revenues supplied by ratepayers is a disservice to ratepayers. The Commission accordingly adopts the AG/AARP adjustment on this issue. Furthermore, the Commission notes that this outcome is consistent with how similar revenue is treated for ComEd's revenue requirement calculation.

VIII. RATE OF RETURN

The parties agree that Rate MAP-P properly applies an authorized rate of return on common equity of 10.05%, which equals the monthly average 4.25% 30-year United States Treasury bond yield during the subject year plus 580 basis points, as set forth in Section 16-0108.5(c)(3) of the Act. They also agree that Section 16-108.5(c)(2) provides that the formula rate approved by the Commission shall "[r]eflect the utility's actual capital structure for the applicable calendar year, excluding goodwill, subject to a determination of prudence and reasonableness consistent with Commission practice and law." Although Section 16-108.5 effectively disconnects capital structure from rate of return, Staff and IIEC are still concerned that AIC has overestimated the proportion of common equity in its capital structure. AIC and Staff propose the following capital structures reflecting their respective recommendations:

	AIC	Staff
Common Equity	54.30%	51.49%
Preferred Stock	1.50%	2.45%
Long-Term Debt	44.20%	46.06%
Short-Term Debt	0%	0%
	100.00%	100.00%

A. Year-End versus Average Capital Structure

1. AIC Position

AIC interprets Section 16-108.5(c) of the Act as requiring the use of its year-end capital structure. AIC states further that under Section 16-108.5(c) the data that it is required to file demonstrating its actual capital structure must be "based on its most recently filed FERC Form 1." AIC notes further that use of a year-end capital structure is more consistent with Commission practice and past orders, and accurately measures a company's earned rate of return on common equity.

AIC is not persuaded by Staff's arguments for use of an average capital structure. Because the Commission has the authority to review a utility's capital structure for prudence and reasonableness, AIC does not share Staff witness Phipps' concern that a utility may manipulate the capital structure through the use of a single day's measurement. Ms. Phipps' example of a utility purposefully delaying a dividend from one year to the next in order to boost the common equity ratio does not sway AIC because according to AIC the Commission could find that a utility's deliberate delay of a dividend was not prudent or reasonable, and could adjust the capital structure to reverse any effects of the delay. AIC argues that the proposed use of an average capital structure solves a problem that does not exist, and merely introduces more complexity into the determination of the capital structure. AIC states further that an "average" capital structure is not an "actual" capital structure. Moreover, AIC alleges that Ms. Phipps calculated the average 2010 capital structure using the monthly balances for 2009 and 2010, and thus Staff's approach uses 2009 data to comply with the statute's mandate that the actual 2010 capital structure be used. AIC concludes that the Commission should apply the clear language and intent of the Act and adopt a year-end capital structure. If the Commission determines that use of an average capital structure is appropriate, AIC suggests that the Commission use an average of beginning and year-end balances for the subject period.

2. Staff Position

Staff recommends establishing formula rates using an average 2010 capital structure comprising 51.49% common equity, 46.06% long-term debt, and 2.45% preferred stock. Staff recommends that the Commission adopt a formula rate methodology that calculates average balances of net short-term debt, long-term debt, preferred stock, and common equity in accordance with Sections 285.4000(b) and 285.4020 of Part 285. Staff witness Phipps explains that average capital structures are less sensitive to manipulation than capital structures measured on a single date. Furthermore, Staff argues that an average capital structure would produce a more accurate measure of a company's earned rate of return on common equity for a calendar year, which is required for the purpose of determining customer surcharges or refunds under Section 16-108.5(c)(5).

In response to AIC's claim that an average capital structure is not an actual capital structure, Staff contends that AIC is simply wrong. Staff notes that the Commission's past practices and own rules recognize that the capital structure components may be measured using average balances. (See Section 285.4000(b)) Furthermore, Staff states that the statute refers to "calendar year," which AIC recognizes as the period from January 1st through December 31st. Staff points out that although Section 16-108.5(c)(2) of the Act specifies that rates reflect the utility's actual capital structure for the applicable year, it does not specify a measurement methodology for capital structure.

Staff finds AIC's claim that Staff uses 2009 data absurd given that the December 31, 2009 balances used by Staff are identical to opening January 1, 2010 balances. Moreover, Staff asserts that AIC's argument is disingenuous. As shown on AIC Ex. 2.2 (Rev.), Workpaper 12 at 158, AIC itself used the December 31, 2009 short-term debt balance in its monthly average net short-term debt calculation. Staff also observes that this is the methodology set forth in Section 285.4000(b), which states, "[e]ach monthly average shall equal the simple average of the beginning and ending monthly balances." Similarly, Staff continues, former Section 16-111(e) of the Act required calculating an average return on equity ("ROE") as follows:

> . . . (a) If the 2-year average of an electric utility's earned rate of return on common equity, calculated as its net income applicable to common stock divided by the average of its beginning and ending balances of common equity using data reported in the electric utility's Form 1 report to the Federal Energy Regulatory Commission.

FERC Form 1 does not contain any balances that are explicitly labeled as "beginning." (See AIC's 2010 FERC Form 1 balance sheet at 110 113) As a consequence, based on the language in the statute, Staff believes that the General Assembly obviously recognized that an end of year balance for the prior year is synonymous with the beginning balance for the current year. Moreover, since there are 365 days between December 31, 2009 and December 31, 2010, Staff observes that using two year-end balances clearly results in a one-year average balance.

Staff agrees with AIC that the Commission has the authority to review a utility's capital structure for prudence and reasonableness, but does not agree that such authority renders Staff's concerns over capital structure manipulation meaningless. According to Staff, AIC's argument ignores the reality that assessing the prudence or reasonableness of the timing of debt and equity financing is problematic because outside parties would be hard-pressed to refute a utility assertion that the utility changed the date of a debt issuance by a few weeks or months because of capital market conditions. For example, despite issuing debt at possibly the worst time in October 2008, no party challenged the timing of AmerenIP's 9.75% $400 million bond issue. (See Docket Nos. 09-0306 et al. (Cons.), April 29, 2012 Order at 139-143) Staff illustrated in testimony how transactions as ordinary as issuing $100 million long-term debt to replace short-term debt, or conversely, using $100 million short-term debt to bridge long-term financing can affect a year-end capital structure, especially if those transactions happen towards the end of the year. (See Staff Ex. 16.0 at 3-7)

Staff recognizes that its proposal to use average capital structures for formula rates would not make it impossible to manipulate capital structures for ratemaking purposes. Since the average comprises thirteen observations, Staff contends that any single month-end balance has less influence on the average. In other words, the manipulation of capital structure through the timing of capital issuances and retirements would have a smaller effect on a capital structure comprising average balances than a capital structure comprising single, end-of-year balances.

AIC asserts that use of a year-end capital structure accurately measures a company's earned rate of ROE. To the contrary, Staff explained that average capital structures would more accurately measure AIC's earned rate of ROE than capital structures measured on a single date for reconciliation purposes. AIC proposes to calculate the rate of return on common equity for reconciliations as D(elivery)S(ervice) ROE = DS Net Income / DS Common Equity Balance. The numerator, "DS Net Income," represents earnings during the calendar year. AIC's proposal would measure the denominator, "DS Common Equity Balance," at a single point in time – the last day of the calendar year. As such, Staff contends that the denominator would misstate the amount of common equity that AIC had invested during the 12 months over which AIC generated the net income reflected in the numerator. Moreover, Staff notes that Standard & Poor's ("S&P") uses average common equity in its calculation of return on common equity and financial literature recognizes that it is "common regulatory practice" to calculate a rate of return on average book equity.

Staff relates further that in Docket No. 11-0721, the Commission adopted an average capital structure instead of a year-end capital structure, stating:

> The Commission concludes that Staff's proposed average capital structure which will calculate the average short-term debt balance, the average balance and embedded cost of long-term debt, and the average common equity balance more accurately reflects the Company's actual capital structure. Staff's proposal is also more consistent with Commission practice and law than the actual year-end capital structure proposed by the Company. The Commission further agrees with Staff that an average capital structure for setting formula rates more accurately measures a company's earned rate of return on common equity for a calendar year and is less sensitive to manipulation than end of year measurement dates. (Docket No. 11-0721,May 29, 2012 Order at 123)

Staff maintains that AIC has offered no cogent reason for the Commission to treat it differently than ComEd on this matter. For all the foregoing reasons, Staff urges the Commission to adopt its methodology for calculating an average capital structure for formula rates and reject AIC's proposal to determine formula rates using a year-end capital structure.

3. Commercial Group Position

The Commercial Group observes that the Commission reached a conclusion on average versus year-end capital structure in Docket No. 11-0721 (May 29, 2012 Order at 123) similar to the decision it reached on rate base. The primary consideration, the Commercial Group continues, is that the reconciliation capital structure reflects what that structure had been throughout the statutory "calendar year" and not at the end of that year. The Commercial Group states that its arguments supporting use of an average rate base are also relevant to the decision on capital structure.

4. Commission Conclusion

Section 16-108.5(c)(2) requires that the formula rates "[r]eflect the utility's actual capital structure for the applicable calendar year, excluding goodwill, subject to a determination of prudence and reasonableness consistent with Commission practice and law." The Act does not specify exactly how the "actual capital structure" is to be determined. The Commission finds Staff's arguments for how to determine AIC's capital structure persuasive. Staff's method is consistent with Commission practice and law and mitigates the risk of manipulation. AIC's claim that Staff uses 2009 data is not well taken given that the December 31, 2009 balances used by Staff are identical to opening January 1, 2010 balances. AIC's argument is also disingenuous in light of its own use of December 31, 2009 data for calculating short-term debt balances. Accordingly, the Commission adopts Staff’s proposed average capital structure methodology with the knowledge that it will more accurately reflect AIC's actual capital structure.

B. CWIP Accruing AFUDC Adjustment

1. Staff Position

Staff recommends an adjustment to the average balances of long-term debt, preferred stock, and common equity to remove the portions already reflected in the AFUDC rate. The Commission’s formula for calculating AFUDC assumes short-term debt is the first source of funds financing CWIP; however, it is not necessarily the only source. That formula also assumes any CWIP not funded by short-term debt is funded proportionately by the remaining sources of capital (i.e., preferred stock, long-term debt, and common equity). Thus, to avoid double counting the portions of long-term debt and common equity that the AFUDC formula assumes is financing CWIP, Staff recommends subtracting $1,160,828 from the preferred stock balance, $21,823,575 from the long-term debt balance, and $24,396,349 from the common equity balance.

Staff relates that AIC had a higher balance of CWIP than short-term debt every month from December 2009 through December 2010. Therefore, Staff states that the AFUDC formula assumes that long-term sources of capital fund CWIP during those months. After removing the portion of short-term debt reflected in the AFUDC calculation, any remaining amount of CWIP accruing AFUDC is allocated to long-term sources of capital based on their proportions to total long-term capital. Staff reports that AIC had no short-term debt during 2010, thus, the 2010 AFUDC rate wholly comprises the costs of long-term debt, preferred stock, and common equity, weighted in the same proportions that they compose total capital. Consequently, Staff observes, the above adjustments do not affect the capital structure ratios that will be applied to rate base for 2010. Nevertheless, because the Commission will establish a capital structure methodology for future formula rate proceedings and given that AIC's usage of short-term debt during the period formula rates are effective could affect the remaining capital assigned to rate base, Staff explains that capital structure methodology should include Staff's AFUDC-related adjustments to the long-term components to the capital structure. Staff notes that AIC agreed to Staff's CWIP adjustment in Docket No. 11-0282. Staff states further that its position is consistent with the Commission's conclusions in Docket Nos. 95-0076, 08-0363, and most recently 11-0721. Staff asserts that AIC has offered no cogent reason for it to be treated differently than ComEd on this matter and encourages the Commission to adopt the Staff position.

2. AIC Position

AIC acknowledges that since it had no short-term debt during 2010, the 2010 AFUDC rate wholly comprises the costs of long-term debt, preferred stock, and common equity, weighted in the same proportions that they compose total capital. That being the case, AIC points out that Staff's adjustments do not affect the capital structure ratios that will be applied to rate base for 2010. AIC witness Martin testifies that these adjustments are without real purpose or effect. Because these adjustments do not affect the capital structure ratios or rate of return or any other component of the initial rates, Mr. Martin maintains that there is no reason to make the adjustments.

3. Commission Conclusion

The Commission disagrees with AIC's position that the dollar values reflected in its capital structure are meaningless. While under current circumstances, Staff's adjustment will not alter the ratios or rate of return, the Commission finds merit in ensuring that the capital structure is measured accurately. Consistent with Docket No. 11-0721, the Commission adopts Staff's adjustments on this issue.

C. Common Equity Balance - Purchase Accounting

1. Staff Position

In addition to subtracting the portion of common equity that the AFUDC formula assumes is financing CWIP, Staff proposes to subtract the amount of common equity invested in Ameren Energy Resources Generating Company ("AERG") from AIC's average 2010 common equity balance. Staff states that this adjustment, which removes any incremental increase in cost of capital resulting from AIC's affiliation with non-utility companies as required under Section 9-230 of the Act, should not be necessary in future formula ratemaking proceedings since AmerenCILCO transferred AERG to a non-utility subsidiary of Ameren in October 2010.

Additionally, Staff recommends subtracting from the common equity balance the sum of (1) purchase accounting adjustments that are collapsed into Account 114 - Electric Plant Acquisition Adjustments (as identified on AIC's 2010 Form 21 at page 13) and (2) income statement purchase accounting adjustments, which flowed through to retained earnings. Those purchase accounting adjustments, Staff states, did not result in a single dollar of expenditure on utility plant or service. Rather, Staff continues, they represent a re-evaluation of utility assets and liabilities that were already in place and, as such, are inconsistent with a rate setting procedure based on original cost rather than fair value.

Staff understands that AIC does not dispute Staff's explanation of purchase accounting adjustments, yet it still opposes Staff's proposed adjustment to remove from the common equity balance approximately $100 million of retained earnings that AIC claims were generated by purchase accounting. AIC witness Stafford asserts:

> Ameren Illinois issued dividends that reduced the retained earnings that resulted from purchase accounting and recorded the same in accordance with applicable accounting rules. A dividend results in credit to cash and a corresponding reduction to retained earnings, which is a component of stockholder equity….The retained earnings adjustment was effectively eliminated through the payment of common dividends ($61M in 2007 and $60M in 2008) out of net income available to common shareholders. (AIC Ex. 13.4 at 1-2)

Staff disagrees with the claim that paying dividends can eliminate purchase accounting adjustments to net income. Staff explains this could only be true if the purchase accounting adjustments to net income were a necessary condition for AmerenIP to pay a portion of its common dividends, which is incorrect. In other words, Staff points out that AIC's common dividends were paid from cash, and as such, dividend payments decrease the amount of funds available for investment. In contrast, Staff continues, purchase accounting adjustments, including those to net income, do not represent either changes in funds (i.e., cash) available for investment or the generation of cash. That is, AIC cannot invest funds "generated" by purchase accounting in utility plant or distribute those funds to investors in the form of common dividends. Staff contends that this concept is illustrated in AIC's cash flow statement, which subtracts purchase accounting adjustments from net income to calculate cash from operations, whereas common dividend payments reduce cash.

Furthermore, Staff maintains that the lines separating the common equity components – i.e., paid in capital and retained earnings – are permeable. To demonstrate its point, Staff notes that in 1998 IP implemented a quasi-reorganization that eliminated a retained earnings deficit. As explained in IP's 1999 Form 10-K:

> A quasi-reorganization involves restating a company's assets and liabilities to their fair values, with the net amount of these adjustments added to or deducted from the deficit. Any balance in the retained earnings account is then eliminated by a transfer from common stock equity, giving the Company a "fresh start" with a zero balance in retained earnings.

Similarly, from 2007 through 2009, Staff reports that AmerenIP reduced capital available for investment through the payment of common dividends totaling $152 million, which was recorded as a reduction to the retained earnings component of common equity. Immediately thereafter, beginning in the first quarter of 2009, Ameren contributed $155 million to AmerenIP, which was recorded as an increase in the paid in capital component of common equity. The contributed capital (i.e., equity infusions) effectively returned to AmerenIP the $152 million capital that AmerenIP had distributed to Ameren through the common dividend payments, with a net increase of $4 million to AmerenIP's common equity balance. That is, with the combination of AmerenIP common dividend payments by Ameren and the offsetting equity infusions of Ameren to AmerenIP, Staff states that AIC essentially transferred retained earnings balance to paid in capital.

Staff understands AIC to claim that it follows Generally Accepted Accounting Principles ("GAAP") and FASB methodologies among other applicable accounting standards with respect to the recording of common dividend payments. Specifically, AIC assigned first quarter 2005 dividend payments to 2004 purchase accounting earnings first, before allocating remaining 2005 dividend payments between purchase accounting and non-purchase accounting earnings, and all dividends in 2007 and 2008 to purchase accounting earnings first. But despite AIC's claims regarding its accounting practices, Staff asserts that AIC does not and can not cite to a provision in the Commission's USOA or a FASB proclamation that directs utilities to assign (1) earnings to "purchase accounting" and "non-purchase accounting" accounts or sub-accounts; or (2) common dividends to purchase accounting-related net income first and non-purchase accounting-related net income second.

AIC attempts to justify its claim that making common dividend payments would have been impossible if not for the purchase accounting adjustments by arguing that Section 7-103 of the Act prohibits making dividend payments when the retained earnings balance is less than zero. According to Staff, AIC misinterprets Section 7-103. While it is true that Section 7-103(2) of the Act sets forth certain conditions that must be met before dividends can be paid, including a "sufficient earned surplus," Staff points out that the final paragraph of Section 7-103(2) makes clear that those conditions limit only the dividends a utility may pay without Commission approval.

While it is arguable that a positive retained earnings balance is a necessary condition for a utility to pay dividends without Commission authorization, Staff states that the Commission has the power to authorize the payment of dividends even when a utility's balance of retained earnings is negative. For example, in Docket No. 92-0415, Staff relates that IP requested and received Commission authority under Section 7-103 of the Act to declare and pay quarterly dividends on preferred and common stock despite a possible negative retained earnings balance. In conclusion, Staff recommends the Commission adopt its proposed adjustment to remove all purchase accounting adjustments, including goodwill, from AIC's common equity balance.

Staff denies that it is challenging the Commission's decision in Docket No. 04-0294 as it pertains to the calculation of capital structure. In Docket No. 04-0294, Staff explains that the Commission adopted its recommendation to collapse the impact of push down accounting into Account 114 - Electric Plant Acquisition Adjustments for all Illinois regulatory purposes, such as reporting in Form 21 ILCC annual reports. (See September 22, 2004 Order at 33-34) Staff avers that its adjustment, which removes all purchase accounting adjustments, including goodwill, that are included in Account 114, as well as income statement purchase accounting adjustments that are reflected in the retained earnings balance, complies with the reporting requirements set forth in the Commission's Order in Docket No. 04-0294. Although AIC's argument implies that Account 114 includes the net income-related purchase accounting adjustments that are reflected in AIC's retained earnings balance, Staff states that the purchase accounting adjustments reflected in Account 114 are separate from the income statement purchase accounting adjustments. Staff relates that this is evident given that the USOA identifies retained earnings as Accounts 215, 215.1, and 216. Staff reports that those accounts are not reflected on page 13 of AIC's 2010 Form 21 ILCC annual report, which summarizes the purchase accounting adjustments collapsed into Account 114. (See AIC 2010 ILCC Form 21 at 13)

Staff also disagrees with AIC's assertion that Staff's position in this case is the same as Staff's argument in Docket No. 11-0282. Staff explains that in Docket No. 11-0282, Staff proposed to remove the goodwill balance in lieu of AIC's purchase accounting adjustment balance to avoid including in rates any purchase accounting adjustments that are not appropriate for ratemaking purposes. According to Staff, the net income related adjustment to retained earnings was introduced during the evidentiary hearing in that case, when Staff discovered that in Docket Nos. 07-0585 et al. (Cons.), AIC made two purchase accounting adjustments to AmerenIP's common equity balance: the first adjustment subtracted $155 million of goodwill net of purchase accounting adjustments (i.e., the Account 114 balance); the second adjustment subtracted $63 million of income generated from purchase accounting. In the 2011 rate case, AIC testified it would make that adjustment until the retained earnings from income generated from purchase accounting had been fully paid out as common dividends. Staff therefore concludes that there is neither a dispute about whether the balance in Account 114 should be subtracted from AIC's balance of common equity nor the correct balance in Account 114. Staff states that any AIC argument that suggests otherwise is a straw man.

Staff believes that AIC misconstrues the point of Staff's summary regarding dividend payments and equity infusions from the date Ameren acquired IP through the end of year 2010. While AIC argues that it is impossible for AmerenIP to have paid $76 million in common dividends out of retained earnings to Ameren without net income generated as a result of purchase accounting, Staff notes that AIC's argument assumes that common dividends can only be assigned to the retained earnings component of common equity. Although it is true that common dividends are subtracted from retained earnings, Staff states that amounts can and have been transferred from retained earnings to other common stock accounts and vice versa. Further, Staff observes that there is no distinction between common equity components from a financial standpoint. Staff points out that the balance of retained earnings does not have a distinct, different rate of return than other components of common equity. Staff contends that it is nothing but a contrivance of accounting when common equity flows from a parent to subsidiary are recorded in the subsidiary's paid in capital account but common equity flows from the subsidiary to the parent (i.e., dividends) are recorded in the subsidiary's retained earnings account. Staff asserts that the fact is that from the date of Ameren's acquisition of IP in October 2004 through 2010, AmerenIP has received nearly as much common equity capital from Ameren as AmerenIP has returned to Ameren through dividends.

2. AIC Position

AIC adjusts its common equity balance by subtracting $350,833,352 for the purpose of calculating capital structure in a manner that excludes the effects of purchase accounting. The purchase accounting at issue relates to Ameren's 2004 acquisition of IP in Docket No. 04-0294. Staff recommends an additional reduction to equity of approximately $101 million. AIC agrees that all effects of purchase accounting should be removed for all ratemaking purposes. AIC maintains that Staff's adjustment and associated methodology do not accomplish this end and leave certain purchase accounting in place while eliminating others. AIC argues further that Staff's proposed treatment of purchase accounting is asymmetrical and unfairly prejudices AIC.

a. Consistency with Docket No. 04-0294 and Docket No. 11-0282

In developing the capital structure for ratemaking purposes in this proceeding, AIC states that it reversed all purchase accounting in compliance with the Commission's Order in Docket No. 04-0294; which in addition to approving Ameren's acquisition of IP, also approved the proper accounting for all regulatory purposes that followed. AIC claims that Staff's adjustment does not comport with the Order in Docket No. 04-0294 because it does not remove all purchase accounting associated with Ameren's acquisition of IP.

"Purchase accounting" is a term that is used throughout this proceeding, and the specific meaning depends on the context. In this context, AIC asserts that it relates to the accounting entries that were made pursuant to applicable accounting standards at the time of IP's acquisition. Accounting standards required that AIC "push down" any investment onto IP's books, and also required that AIC adjust both assets and liabilities to fair market value. Because the Commission sets rates based upon the original book value of plant in service, altering of account balances to reflect market value gave rise to concern. Therefore, in order to maintain accounting of the cost basis for IP in a manner neutral to the change in corporate ownership, AIC relates that the Commission ordered that all purchase accounting be reversed. Further, Staff recommended that Ameren "collapse" all accounting entries into Account 114. Ameren agreed, and the Commission approved the recommended accounting for "all Illinois regulatory purposes." (Docket No. 04-0294, September 22, 2004 Order at 33-34) AIC acknowledges that the intent of the Commission's requirement to "collapse" all accounting entries into one account is not expressly stated in the Order, but the purpose is fairly obvious; rather than adjusting several account balances to reverse all purchase accounting, AIC asserts that it is instructed to combine the sum total of all various adjustments and record them in Account 114. Accordingly, AIC explains, the effect of the Commission's Order is that the elimination of goodwill from the common equity balance must be netted against all other purchase accounting entries. In this manner, purchase accounting and goodwill are intertwined. (See also Docket No. 11-0282, January 10, 2012 Order at 53-54) AIC witness Stafford also testifies that this regulatory accounting has been consistently followed and applied in rate cases subsequent to the acquisition. He notes further that the Commission expressly affirmed AIC's treatment of purchase accounting for calculating capital structure in Docket No. 11-0282. (Order at 53-54)

In contrast to its proposal, AIC contends that Staff's recommendation simply cannot be implemented without running afoul of the Commission's decision in Docket No. 04-0294. Staff's position, Mr. Stafford explains, is in conflict with the Commission's directive that all purchase accounting be collapsed into Account 114 for "all regulatory purposes," a requirement that necessitates the removal of goodwill net of all other combined purchase accounting. AIC recognizes that Staff witness Phipps revised her initial proposal later in her testimony, but suggests that her prepared direct testimony may be relied upon to illustrate Staff's methodology. In explaining her initial proposal, she articulates the two-step process she used to develop her adjustment of approximately $450 million dollars to the common equity balance. She starts with AIC's full purchase accounting adjustment, and then adds back income statement purchase accounting adjustments that flowed through retained earnings. AIC argues that what she is doing is in effect reversing the "collapsing" of purchase accounting entries, including retained earnings balances from previous periods, without consideration of whether such earnings are still retained by AIC, and leaving the effects of the push down accounting partially in place to calculate her proposed capital structure. AIC insists that Staff's methodology is not consistent with the Order in Docket No. 04-0294. Additionally, in affirming AIC's position in Docket No. 11-0282, AIC observes that the Commission found "the record supports AIC's position that purchase accounting and goodwill are intertwined . . . This adjustment reflects a netting of accounting adjustments against the goodwill balance which is supported by the record of this proceeding." (Order at 54)

b. Staff's "Transfer" Theory

In rebuttal testimony, Staff argues that dividends and equity infusions occurring in 2007 through 2009 effectuated a transfer of purchase accounting from one category of common equity to another, i.e., from retained earnings to paid-in capital. As a threshold matter, AIC is uncertain how Staff's argument squarely responds to AIC's position or, for that matter, supports Staff's position to eliminate purchase accounting reversals other than goodwill. AIC asserts that Staff simply does not offer an analysis that articulates a coherent explanation as to the salience of its theory, nor does it explain why its adjustment offers an appropriate remedy. Notwithstanding, AIC insists that the facts affirmatively demonstrate there was no “transfer” of dividends to paid-in capital as Staff alleges.

Staff’s argument hinges upon the general observation that AmerenIP issued dividends in 2007 and 2008 and received equity infusions in 2009. But according to AIC, the dividends and equity infusions for AmerenIP during that historical period were made in the ordinary course of business, as can be clearly demonstrated by an examination of the historical context of these business activities. In 2004, when Ameren acquired IP from Dynegy, IP was in poor financial condition and was subject to a dividend restriction imposed by the Commission. Upon acquisition, Ameren infused almost $900 million into AmerenIP and, in its Order in Docket No. 04-0294, the Commission removed the dividend restriction after certain criteria were established. In 2007, AmerenIP resumed paying dividends and continued to pay them until late 2008. As demonstrated in the table presented in Mr. Martin’s surrebuttal testimony, all dividends paid by Ameren subsidiaries, including AmerenIP, were used to pay dividends to shareholders. (See AIC Ex. 24.0 at 4) Mr. Martin testifies that in both 2007 and 2008, dividends paid by Ameren subsidiaries, including AmerenIP, equaled exactly the amount paid out to external investors through Ameren dividends. AIC therefore avers that the source of the equity infusions from Ameren to AmerenIP in 2009 could not have come from earlier paid dividends.

Contrary to Staff's assertion, AIC maintains that the facts show that the AmerenIP equity infusion came from three sources: proceeds from Ameren’s public equity offering, proceeds from the sale of Ameren stock under the dividend reinvestment program, and proceeds from the sale of Ameren stock under the 401K program. AIC states that the common stock issuance was a reaction to the financial crises that occurred in the fourth quarter of 2008. Mr. Martin explains that Ameren reacted this way to the financial crises to preserve financial integrity and ensure liquidity. In the first quarter of 2009, Ameren infused $58 million into AmerenIP and also an additional $36 million later that year. AIC states that the infusion was made from proceeds generated in 2009 from an Ameren stock offering that raised $535 million dollars. AIC also notes that Ameren reduced its dividend to external investors in 2009 as well.

As its arguments show, AIC concludes that no purchase accounting “transfer” occurred. AmerenIP resumed paying dividends as permitted by the Commission; the dividends paid to Ameren by AmerenIP in 2007 and 2008 were added to other subsidiary dividends and then paid to external investors as part of Ameren dividends. In other words, AIC states that the dividends were paid out to investors external to Ameren. Prompted by market turmoil in the fourth quarter of 2008, Ameren began to issue stock in 2009 and used part of the proceeds to ensure the financial integrity of AmerenIP through an equity infusion. AIC contends that it is clear that Ameren raised funds external to the company and paid them into AmerenIP for legitimate business purposes. Under these facts, AIC insists that a theory of some sort of improper accounting “transfer” simply cannot be sustained.

Additionally, AIC argues that the accounting characterizations made by Staff in support of its “transfer” allegations are not accurate. According to AIC, Staff does not openly acknowledge in its argument that the level of retained earnings is impacted by income, or, put another way, that the net income, as reported on an income statement, and retained earnings, as stated on a balance sheet, are interrelated values; one affects the other. Because Ameren was required to adjust AmerenIP’s assets and liabilities to fair market value, AIC states that Ameren’s net income is affected by purchase accounting. When income then contributes to retained earnings, AIC contends that purchase accounting reversal is required in accordance with the Order issued in Docket No. 04-0294. When Ameren issues dividends, retained earnings are decreased, and in turn the equity balance is reduced. Therefore, AIC argues that the reversal of the retained earnings for ratemaking purposes is no longer required because the otherwise offsetting equity has been eliminated from Ameren's books. Moreover, AIC insists that Staff’s characterization that dividends are paid from cash, and not retained earnings, is incorrect. Clearly, dividends are paid in cash, but the payment of dividends, AIC continues, reduces retained earnings, which is a component of equity. Additionally, AIC argues that a positive retained earnings balance is a legal pre-condition for the payment of dividends. Therefore, AIC concludes, it cannot be disputed that dividends are paid out of retained earnings. Furthermore, AIC maintains that Staff’s contention that the “lines separating the components of common equity ... are permeable” is simply not true. (Staff Ex. 16.0 at 15) AIC asserts that accounting standards require that dividends paid by Ameren be recorded as a reduction to retained earnings. Mr. Stafford also notes that no basis exists under GAAP or the USOA to support Staff’s position.

c. Compliance with Section 16-108.5

Section 16-108.5(c)(2) requires that the capital structure “reflect the utilities actual capital structure for the applicable calendar year, excluding goodwill, subject to a determination of prudence and reasonableness consistent with Commission practice and law.” Consistent with Docket Nos. 04-0294 and 11-0282, AIC states that it has excluded goodwill from its capital structure as well as all other purchase accounting adjustments as a result of collapsing all purchase accounting adjustments together. AIC argues that nothing in Section 16-108.5 invalidates the orders in prior dockets. To the contrary, AIC continues, the law directs it to continue to follow the Commission approved accounting ordered in 2004 and applied since that time.

d. Unchallenged Calculation

As AIC understands it, Staff does not challenge AIC’s accounting on this issue, but rather challenges AIC's ratemaking treatment of purchase accounting adjustments. Given this understanding and Staff's acknowledgment that AIC’s accounting is a result of the Commission’s Order issued in Docket No. 04-0294, AIC views Staff as in essence challenging the Commission’s decision in Docket No. 04-0294 as it pertains to the calculation of capital structure. AIC urges the Commission to follow the accounting it established for calculating capital structure and approve AIC’s proposed common equity balance. AIC argues that the Commission should do so not only for the sake of consistency and fairness, but also because the ordered accounting treatment ensures removal of all purchase accounting for all regulatory purposes in a neutral manner, thus ensuring continuity of application and proper synchronization with all other regulatory accounting.

3. Commission Conclusion

The Commission finds this to be an extremely complicated issue and despite the best efforts of the parties, difficult to understand. It appears to the Commission that Staff is essentially concerned that AIC has engaged in accounting transactions that allowed it to manipulate its common equity balance. For example, Staff contends that it is nothing but a contrivance of accounting when common equity flows from a parent to subsidiary are recorded in the subsidiary's paid in capital account but common equity flows from the subsidiary to the parent (i.e., dividends) are recorded in the subsidiary's retained earnings account. Staff asserts that the fact is that from the date of Ameren's acquisition of IP in October 2004 through 2010, AmerenIP has received nearly as much common equity capital from Ameren as AmerenIP has returned to Ameren through dividends.

The Commission has attempted to review the record carefully and cannot find an instance where AIC has violated any accounting rules. As the Commission understands it, accounting rules exist, in part, to protect the veracity of companies' financial statements. Because it appears that AIC has followed all accounting rules and Commission Orders relating to its accounting for purchase accounting, or push down accounting, the Commission rejects Staff's proposed adjustment to common equity balance. A separate issue addressed elsewhere in this Order is whether the proportion of common equity in AIC's capital structure is reasonable and prudent.

D. Subsequent Discussions/Report on Capital Structure

1. Staff Position

While Staff believes its own proposed capital structure is appropriate in the current proceeding, it also suggests that it is probable that a capital structure containing that same level of common equity would not be prudent and reasonable in future formula rate proceedings. Thus, Staff recommends that the Commission order AIC to work with Staff to explore more leveraged capital structures for future years and subsequently provide a report to the Commission with its 2013 formula rate filing. Whether Staff would expect such negotiations to result in a consensus on what constitutes an appropriate capital structure is unclear.

2. IIEC Position

IIEC recognizes that the Commission adopted a similar proposal concerning future capital structure discussions in ComEd's recent formula rate case, Docket No. 11-0721. (Order at 134) IIEC has no objection to discussing a more leveraged capital structure for AIC, including the appropriate cap for the ratio of common equity to total capital. IIEC asserts that any such discussion should provide an opportunity for all parties to participate and should not be a substitute for insertion of the 50% common equity ratio cap into Rate MAP-P pending final resolution of this matter. When the Commission conducts its review, IIEC contends that the outcome should reflect the reduced operating risk realized by AIC as the result of the existence of the formula rate, as well as all other factors relevant to establishing an appropriate level of common equity. IIEC adds that any ceiling on the common equity ratio developed as a result of such discussions should apply to the pertinent rate year in future formula rate filings.

While IIEC believes that it is at least implied in the conclusion concerning ComEd's future capital structure discussions, IIEC urges the Commission to make clear in this docket that other parties may participate in the discussions on a more leveraged capital structure for AIC. IIEC believes it is important to allow other parties to participate because under Public Acts 97-0616 and 97-0646, a hearing on a formula rate filing will not occur unless the Commission deems one necessary. Therefore, parties may not be permitted to influence the development of a more leveraged capital structure on a going forward basis unless they are allowed to participate in the discussion between Staff and AIC. Even if a later opportunity is available in a formal hearing on AIC's 2013 formula rate filing, IIEC fears that the abbreviated schedule for the proceeding would compromise other parties' time to contribute to the determination of the capital structure. IIEC recommends that the Commission allow other parties to participate in the discussions with Staff and AIC and take part in the preparation of any report to the Commission.

3. AIC Position

AIC understands Staff to believe that the capital structure presented by AIC in this proceeding may not be prudent and reasonable on a going-forward basis in light of changes in operating risk that may be affected by Public Acts 97-0616 and 97-0646. To address this concern, AIC agrees with Staff that it would be useful to explore and discuss particular issues surrounding the composition of AIC's capital structure outside the context of a contested proceeding. AIC is also agreeable to providing a report to the Commission with its 2013 formula rate filing, with the caveat that AIC and the Staff are not required to reach a consensus with respect to capital structure issues discussed by them.

AIC objects to the notion that other parties be allowed to participate in its capital structure discussions with Staff. AIC contends that IIEC had an opportunity to define such a process earlier in this case and characterizes IIEC's position on this issue as vague. AIC asserts that there is a schedule for testimony for a reason, and it is to develop a full record. Eleventh-hour legerdemain in a brief, AIC argues, is no substitute for a proper evidentiary presentation. AIC recommends that the Commission reject IIEC’s effort to transform Staff’s proposal into something else more formal and broader in scope.

4. Commission Conclusion

As in Docket No. 11-0721, the Commission supports the concept of discussing outside of a formal proceeding a more leveraged capital structure for AIC as well as AIC's inclusion of a report on those efforts with its 2013 formula rate filing. While consensus on the capital structure issues is certainly desirable, the Commission does not believe it is practical or appropriate to require consensus at the end of what are essentially settlement negotiations. As for whether others should be allowed to participate, the Commission agrees with IIEC that it would be appropriate to provide other parties the opportunity to do so. Although AIC has expressed concerns about expanding participation, neglecting to do so will hamper efforts to resolve issues if a formal hearing is eventually held on the associated formula rate plan since parties to such a hearing may raise objections to whatever Staff and AIC determine. While the addition of other parties may lead to other issues being raised and/or hinder the resolution of issues, if any issues are resolved or at least narrowed, some benefit from the discussions will emerge. Accordingly, the Commission directs Staff and AIC and welcomes other interested parties to participate in informal discussions concerning AIC's capital structure. Following those discussions, AIC shall include with its 2013 formula rate filing a report on those efforts.

E. Common Equity Ratio/Cap Limit

1. IIEC Position

AIC proposes to use its actual capital structure as of December 31, 2010, excluding goodwill. IIEC, however, finds this capital structure too heavily weighted with common equity and therefore believes that it overstates AIC’s reasonable cost of capital. IIEC notes that under the Act, the Commission must determine if AIC’s proposed capital structure is prudent and reasonable. But according to IIEC, AIC has not presented testimony in this case that allows the Commission to make that determination. In addition, under Section 16-108.5(d), IIEC notes that the Commission has only 45 days to review the utility’s annual reconciliation filing and determine whether or not it will conduct a hearing on the filing. Under such circumstances, IIEC argues that the Commission should implement procedures to ensure that in evaluating AIC’s capital structure, the capital structure does not contain an excessive amount of common equity, as the capital structure proposed by AIC in this case does. Therefore, IIEC recommends that the Commission order that the AIC formula rate reflect a common equity ratio limit of 50% to ensure that AIC’s overall cost of capital reflects reasonable and prudent management of its capital structure.

Under IIEC’s proposal, if AIC’s actual common equity ratio is greater than 50%, it would be required to prove in a hearing that its actual capital structure is prudent and reasonable and, therefore, appropriate for use in Rate MAP-P. To the extent AIC fails to prove that such a capital structure is reasonable, then Rate MAP-P would be developed using a capital structure with a common equity ratio of 50%. IIEC recommends that the Commission investigate an appropriate common equity ratio limit at least every three years. IIEC states that the difference between the 50% and the 54.28% common equity ratio proposed by AIC or the 51.49% common equity ratio proposed by Staff, should be allocated to a debt component of the capital structure of whichever capital structure is ultimately approved by the Commission.

IIEC contends that use of a 50% common equity ratio cap is appropriate for several reasons. First, IIEC believes that it will help ensure that AIC recovers only its prudent and reasonable capital costs. A capital structure too heavily weighted with common equity overstates AIC’s reasonable cost of capital and, therefore, would be imprudent and unreasonable. The record in this docket, IIEC maintains, establishes that the capital structures proposed in this case by AIC and Staff each contain so much common equity that they may not be prudent and reasonable on a going-forward basis. Under such circumstances, IIEC asserts that the imposition of the 50% common equity cap would be appropriate.

Second, IIEC believes that a 50% common equity ratio cap is appropriate because it exceeds the common equity ratio authorized for the old AIC operating subsidiaries in AIC’s last fully litigated electric rate case (AmerenCILCO - 43.61%; AmerenCIPS - 48.67%, and AmerenIP - 43.55%). Those equity ratios were established under the old ratemaking procedures, which have been supplanted by the implementation of the formula rate process. IIEC states that the new formula rate process mitigates AIC’s operating risks and in turn helps support a stronger credit rating for AIC. This reduced operating risk, IIEC continues, allows AIC to increase its financial risk via reducing its common equity ratio of total capital without a negative impact on its credit rating. Indeed, IIEC observes, S&P views the development of the formula rate process “. . . as potentially enhancing Ameren’s credit quality and demonstrating Ameren’s improving management of its regulatory risk.” (See IIEC Ex. 1.0 at 13 quoting S&P Ratings Direct on Global Credit Portal, Ameren Illinois Co., March 16, 2012 at 2). IIEC reports that Moody’s reached the same conclusion and increased the AIC credit rating largely due to the formula rate law. (See AIC Ex. 24.0 at 9) But even though AIC's credit and bond ratings have improved, IIEC observes that AIC's equity component has increased despite its lower risk. IIEC contends that this change suggests that the incentive to increase equity Staff noted is already having an effect that warrants active oversight.

The third reason that IIEC considers a 50% common equity ratio cap appropriate is that AIC's previously approved capital structures, which contained equity ratios of substantially less than 50%, supported an investment grade bond rating for AIC. Therefore, IIEC avers that a 50% equity ratio should more than adequately perform the same function in this case.

Fourth, IIEC argues that a 50% common equity ratio cap is reasonable because the 50% cap is not an absolute cap on the common equity ratio for AIC. Under the IIEC proposal, AIC would be free to present evidence to the Commission that an equity ratio in excess of 50% was prudent and reasonable. On the other hand, IIEC adds, the 50% is not intended to be a guaranteed equity ratio. IIEC explains that the Commission still has the duty under Section 16-108.5 to determine whether the capital structure presented by AIC for ratemaking purposes is prudent and reasonable regardless of the level of common equity reflected in the capital structure. The Commission would be free under Section 16-108.5 to initiate hearings involving the reasonableness and prudency of any capital structure presented by AIC containing a common equity ratio of less than 50%. IIEC does not intend for its proposal to guarantee that a capital structure with less than 50% common equity would be considered just and reasonable by the Commission. The 50% cap, IIEC points out, would merely operate as a trigger to require a hearing to the extent AIC's actual capital structure contains an equity ratio greater than 50%.

Fifth, IIEC contends that the Commission's rejection of its proposal for a 55% common equity ratio cap for ComEd does not support rejection of IIEC's proposal here. IIEC observes that the Commission rejected its proposal in that case because ComEd's "current common equity ratio of 45.54% makes such a cap unnecessary in this proceeding." (Docket No. 11-0721 Order at 131) In this case, AIC proposes a common equity ratio of 54.28%, well in excess of the 50% cap recommended by IIEC in this case. Furthermore, Staff's common equity ratio of 51.49% exceeds the cap as well. Thus, IIEC observes, the circumstances of this case are substantially different than those in the ComEd case and justify adoption of the 50% cap as proposed by IIEC in this case.

With regard to Staff's position, although Staff argues rigorous oversight of the utility capital structure is required because Section 16-108.5 gives utilities an incentive to increase their common equity, IIEC notes that Staff does not specifically address IIEC's common equity cap/trigger. IIEC states that Staff's proposed common equity ratio of 51.49% reflects the reduced operating risk produced by the new formula rate regime. Staff's proposed capital structure, IIEC concludes, is thus more prudent and more reasonable than AIC's actual capital structure, which does not reflect the reduction in operating risk. Staff also has recognized, IIEC continues, that even the 51.49% common equity ratio it proposes may be higher than necessary under the new formula rate regime.

Under these circumstances, IIEC contends that an investigation of a more leveraged capital structure is appropriate. In the interim, IIEC states that adoption of its 50% of common equity ratio cap or trigger would be appropriate, and provide rigorous oversight of AIC's capital structure. IIEC notes that the cap/trigger is not a hard cap. If exceeded, it would simply trigger a hearing in which the Commission would consider the prudence and reasonableness of AIC's capital structure. As an example, IIEC states that adoption of the 50% cap/trigger would not prevent the Commission from adopting Staff's proposal in this case -- if the Commission found that a capital structure with 51.49% common equity is prudent and reasonable based on the evidence in this case.

2. Staff Position

Staff observes that the authorized rate of return on common equity under the formula rates plan is a function of only two factors: (1) the average yield on 30-year U.S. Treasury bond yields plus 580 basis points, and (2) possible performance penalties. Consequently, the authorized rate of return on common equity does not respond to changes in the common equity ratio. In other words, Staff relates, Section 16-108.5 of the Act severs the inherent link between the rate of return on common equity and the level of financial risk associated with a utility's capital structure. Therefore, absent rigorous Commission oversight of the capital structure, Staff asserts that Section 16-108.5 provides a clear incentive to utilities to increase their respective common equity ratios.

Staff considers it significant that the credit ratings agencies have indicated that the implementation of formula rates will be favorable toward AIC's credit quality and, indeed, Staff points out, it has already resulted in improved credit ratings. Specifically, Moody's notes that the formula rates plan should result in more timely cost recovery, resilient credit metrics, and better ability to earn returns, while helping to substantially offset lingering concerns about the regulatory framework. In addition, S&P states that the new law improves regulatory risk and provides a "streamlined process" for rate setting expected to improve the stability of the utilities' cash flows and ultimately reduce regulatory lag. Therefore, Staff concludes that a capital structure containing as much common equity as the capital structure Staff presented in this proceeding is probably not prudent and reasonable on a going-forward basis.

Nonetheless, Section 16-108.5(c)(2) requires the use of the utility's actual capital structure for the applicable calendar year, excluding goodwill, subject to Article IX generally and a determination of prudence and reasonableness consistent with Commission practice and law. The most recent calendar year for which actual data was available at the time of filing was 2010. Since AIC's 2010 capital structure evolved prior to the reductions in operating risk resulting from the passage of Public Acts 97-0616 and 97-0646, for this proceeding, Staff recommends that the Commission adopt the actual calendar year 2010 capital structure that Staff proposes as adjusted.

In support of its position, Staff states that S&P indicates that AIC's regulated utility operating risk is lower than that of Ameren, which includes significantly riskier generation operations. Given that AIC has lower operating risk than Ameren, Staff avers that AIC should be able to maintain more financial risk (i.e., have a lower common equity ratio) than Ameren to achieve the same stand-alone credit rating as Ameren. Thus, Staff contends that Ameren's common equity ratio of 52.54% represents an upper bound for AIC's equity ratio. Appropriately, Staff's proposed common equity ratio for AIC is slightly lower at 51.49%. AIC's proposal is greater than Ameren's, at 54.28%. If the Commission chose to adopt AIC's proposed capital structure, Staff avers that it would violate Section 9-230 of the Act, which states as follows:

> In determining a reasonable rate of return upon investment for any public utility in any proceeding to establish rates or charges, the Commission shall not include any (i) incremental risk, (ii) increased cost of capital, or (iii) after May 31, 2003, revenue or expense attributed to telephone directory operations, which is the direct or indirect result of the public utility's affiliation with unregulated or nonutility companies.

Staff also compared AIC's capital structure to those of other similarly rated electric companies. Moody's categorizes debt securities on the basis of the risk that a company will default on its interest or principal payment obligations. The resulting credit rating reflects both the operating and financial risks of a utility. As of the end of 2010, AIC had a Moody's corporate credit rating of Baa3 (equivalent to an S&P rating of BBB-), which, as noted above, was recently upgraded to Baa2. Based on data from the S&P Utility Compustat database, the average common equity ratio for utilities in the electric industry with an S&P credit rating in the BBB range equals 47.02%. Staff states that its proposed common equity ratio of 51.49% indicates an appreciably lower degree of financial risk than the average BBB rated electric industry company. Thus, Staff opines that its proposed common equity ratio may be higher than necessary for that rating. Yet, AIC's proposed common equity ratio is even higher still, at 54.28%. According to Staff, this indicates, just as the comparison to Ameren's common equity ratio above, that AIC's proposed common equity ratio is unnecessarily high.

Staff states that AIC's only response to Staff's analysis is to note that "in the last few years, Moody's has expressed concerns about the supportiveness of the regulatory environment in Illinois, which the agency rates at the sub-investment grade Ba level." (AIC Ex. 14.0 at 5) Based on that observation, AIC claims that it "has been required to elevate its common equity ratio to a level greater than that of its parent and other comparably-rated electric utilities." (*Id*.) Staff finds this extrapolated conclusion to be entirely unfounded. First, Staff asserts that AIC presented no analysis or outside corroboration to substantiate the implication that AIC has greater operating risk than Ameren or other comparably-rated utilities. While Staff's analysis compared AIC's risk relative to that of Ameren and other utilities, Staff contends that AIC's response merely attempts to establish the absolute operating risk level of AIC. According to Staff, AIC did not, however, present any information regarding the risks of Ameren and other Baa rated utilities at all. Thus, Staff concludes that AIC undeniably fails to address the critical issue of relative risk, rendering illogical AIC's argument that it must maintain a higher relative equity level. Second, Staff maintains that AIC's attempt to establish the absolute operating risk level of AIC is deficient and biased. Regulatory environment is only one factor affecting operating risk; yet Staff observes that AIC discusses only the effects of that factor to the exclusion of all others. Indeed, despite AIC's regulatory environment, Staff asserts that S&P still concluded that AIC's overall operating risk is lower than that of Ameren. Thus, Staff reiterates that AIC should be able to maintain more financial risk (i.e., have a lower common equity ratio) than Ameren to achieve the same stand-alone credit rating as Ameren. Staff argues that AIC has presented nothing to suggest otherwise.

3. AIC Position

AIC opposes IIEC's recommendation that if AIC's common equity ratio is greater than 50%, AIC should be required to prove that its actual capital structure is reasonable and appropriate. AIC argues that the Commission has ample authority to investigate the prudence of AIC's capital structure annually, and need not set some manufactured, artificial limit masquerading as a "test." According to AIC, IIEC witness Gorman bases his argument solely on his observation that AIC's common equity ratio of 54.28% is higher than the common equity ratios in AIC's 2009 rate case. AIC witness Martin contends that AIC had valid reasons for increasing its common equity ratio since the last electric rate proceeding, and those reasons remain valid. Furthermore, AIC points out that the Commission approved a common equity ratio of 53.27% in AIC's gas rate order issued in January 2012 (Docket No. 11-0282 at 128), which AIC views as affirmation of the reasonableness of the steps it has taken to strengthen its capital structure. AIC notes that Mr. Gorman testified in that case and proposed no adjustments to AIC's capital structure. For such reasons, AIC maintains that Mr. Gorman's selection of 50% is thus arbitrary and unsupported, and its use could jeopardize AIC's credit ratings.

AIC explains that its common equity ratio "evolved" over a number of years prior to this proceeding. A Moody's investment grade credit rating is a strong external, independent indicator of a healthy capital structure. For an investment grade rating in the Baa category, which is the lowest of the four Moody's investment grade credit rating levels, AIC states that Moody's expects a regulated utility's debt to capitalization percentage to be within the range of 45% to 55%. Certain key credit metrics, such as the debt to capitalization ratio, AIC continues, account for only 30% of Moody's overall rating, while 50% of the rating is attributable to (1) the supportiveness of the regulatory framework in which the utility operates and (2) the company's ability to recover costs and earn fair returns within that framework.

Over the last few years, AIC states that Moody's has expressed concerns about the supportiveness of the regulatory environment in Illinois, which the agency has rated at the sub-investment grade Ba level. Given the adverse impact of Moody's assessment and rating of the Illinois regulatory environment on AIC's overall credit rating, AIC contends that it has been important for it to maintain a debt to capital ratio, which accounts for 7.5 percentage points of 30% rating weight assigned to key credit metrics, near the low end of the 45% to 55% range in order to maintain its investment grade rating and ensure access to capital on reasonable terms and conditions. In short, AIC argues that strong credit metrics have been necessary to offset credit rating agency concerns regarding the supportiveness of the Illinois regulatory framework and AIC's ability to recover its cost and earn a reasonable return within such framework and continue to be essential to AIC's maintenance of investment grade credit ratings.

Moody's recently upgraded AIC's issuer rating from Baa3 to Baa2 following a more than three month review process. Certain other AIC ratings were also upgraded by one notch. According to AIC, Moody's cited the new formula rate legislation and expectation of improved cost recovery clarity as factors supporting the upgrade. But AIC also states that Moody's reiterated its concerns regarding AIC's "challenging" regulatory framework and the overall supportiveness of the underlying regulatory environment in Illinois, which Moody's continues to rate below investment grade. Even with the recent passage of formula rate legislation, AIC maintains that regulatory uncertainly and unpredictability in Illinois continues to contribute to a relatively high degree of business risk for AIC. In upgrading its credit rating at this juncture, AIC asserts that Moody's expressly assumes that the utility's regulatory environment and cost recovery prospects do not deteriorate. AIC also understands Moody's to be concerned about Public Acts 97-0616 and 97-0646 being implemented as "intended," the entry of "unsupportive" orders, and "unfavorable or adverse" political intervention in the regulatory process. AIC contends that strong credit metrics, including a healthy capital structure, are necessary to offset rating agency concerns regarding the supportiveness of the regulatory environment and ensure that AIC is able to maintain its investment grade rating.

While the recent rating upgrade is positive, AIC observes that the current rating is still only two notches above junk bond status. At this time, AIC does not believe that the rating upgrade warrants a significant change in its capital structure, particularly in light of ongoing concerns about the implementation and true effect of the new formula rate legislation. Rather, AIC states that it should continue to monitor business and economic conditions and finance opportunities as they arise. In the future, AIC allows that positive credit rating actions that suggest rating agency perceptions of a more stable, predictable, and supportive regulatory environment could justify a fundamental change in the capital structure of AIC, including a change in the targeted equity ratio. At this time, AIC concludes that such a change cannot be justified.

AIC contends that Staff's reliance on Section 9-230 of the Act is misplaced. According to AIC, Staff does not demonstrate how AIC's proposed capital structure would violate Section 9-230 simply because AIC's common equity ratio exceeds that of Ameren. AIC asserts that Section 9-230 addresses situations in which the relatively risky operations of affiliates spill over into the utility's cost of capital and cause the utility to pay more for debt or equity. In other words, Section 9-230 requires that the Commission set the utility's cost of capital as if it were not affiliated with riskier entities. AIC argues that Staff makes no such showing and fails to connect the dots in a way that would show that if AIC were a stand-alone company, it would have a lower cost of capital. AIC states that instead, Staff just points to two dots—AIC's common equity ratio and Ameren's common equity ratio—and contends that a violation of Section 9-230 is present without explaining how. Given the concerns shared by many regarding the implementation of Public Acts 97-0616 and 97-0646, AIC maintains that the Commission should not make premature pronouncements about AIC's capital structure, and certainly should not do so based on a misapplication of Section 9-230 of the Act.

4. Commission Conclusion

Section 16-108.5(c)(2) provides that the formula rate approved by the Commission shall "[r]eflect the utility's actual capital structure for the applicable calendar year, excluding goodwill, subject to a determination of prudence and reasonableness consistent with Commission practice and law." As part of its capital structure, AIC presents its common equity ratio of 54.28% while Staff argues for an adjusted common equity ratio of 51.49%. IIEC recommends using a common equity ratio trigger of 50%, meaning that any capital structure proposed by AIC containing a common equity ratio of more than 50% would automatically result in a closer look by the Commission. If AIC could not justify a common equity ratio of more than 50%, IIEC would have the Commission cap AIC's common equity ratio at 50%.

As an initial matter, the Commission is not inclined to adopt IIEC's proposal on this issue. The Act provides the Commission sufficient freedom to investigate AIC's capital structure as necessary. The fact that limited time exists to review the complicated issues raised in a utility's formula rate filing would not be altered by the adoption of IIEC's proposal.

As for the competing common equity ratios presented by AIC and Staff, the Commission finds merit in Staff's arguments. As noted by Staff, S&P has concluded that AIC’s overall operating risk is lower than that of Ameren. The record also reflects that although it continues to have concerns about the regulatory environment in Illinois, Moody's found that the regulatory environment has improved sufficiently to increase AIC's credit rating. Overall, for the reasons contained in the record, the Commission concurs and finds that AIC has lower operating risk than Ameren and now enjoys a more favorable regulatory environment under Public Acts 97-0616 and 97-0646. These facts warrant an adjustment to AIC's 2010 common equity ratio of 54.28%, which represents circumstances as they were prior to Public Acts 97-0616 and 97-0646 and the benefits ensuing to AIC there under. Accordingly, Staff's common equity ratio of 51.49% represents a reasonably adjusted common equity ratio consistent with Commission practice and law, including Section 9-230 of the Act.

F. Balance and Embedded Cost of Long-Term Debt

Staff proposes to set the cost for $50 million of the 9.75% bonds that AmerenIP issued during October 2008 equal to the cost of long-term debt and set the cost of the AmerenCILCO December 2008 bond issuance equal to 6.76%. Staff relates that these adjustments were adopted by the Commission in AIC’s most recent gas rate case, Docket No. 11-0282. Staff also proposes to calculate the average balance of long-term debt and determine the embedded cost in accordance with the methodology set forth in Section 285.4000(b). Doing so leads Staff to remove the incremental cost increase due to AmerenCIPS’ decision to refinance a $67 million, 5-year intercompany promissory note bearing an interest rate of 4.7% with $61.5 million in 30-year bonds bearing an interest rate of 6.7%. Staff notes that the Commission adopted this adjustment in prior rate cases as well. Staff states that this adjustment will not be necessary in future formula ratemaking proceedings because the 4.7% intercompany note's original maturity date was May 2, 2010.

AIC opposes Staff's adjustment for the intercompany note, asserting that the adjustment is not necessary because AIC is using the 2010 year-end capital structure. AIC explains that a year-end capital structure would reflect the maturity of the AmerenCIPS debt, and no adjustment would be required. But aside from voicing its preference for use of the year-end capital structure, Staff states that AIC offers no cogent justification for the Commission to reverse previous decisions on this matter should an average capital structure be adopted. Staff states that AIC's embedded cost of long-term debt equals 7.44%, as shown on Schedule 16.04. That embedded cost reflects time-weighted cost calculations for carrying value, annual amortization expense, and interest payments as described in Section 285.4000(b) of Part 285. If, however, the Commission concludes that an average capital structure should be used, AIC does not object to Staff's methodology for calculating the balance and embedded cost of long-term debt.

The Commission has considered the record on this matter and concludes that adoption of Staff's position is most appropriate. Earlier in this Order, the Commission determined that using AIC's average capital structure is warranted. Staff's position on this issue is consistent with the use of AIC's average capital structure. Moreover, adoption of Staff's position is consistent with the Commission's treatment of this issue in Docket No. 11-0721.

G. Balance and Embedded Cost of Preferred Stock

AIC proposes to use the year-end balance of preferred stock, consistent with its use of a year-end capital structure. Staff proposes to use the average balance of preferred stock, calculated in accordance with Section 285.4000(b) of Part 285. Although AIC believes that a year-end capital structure should be used, if the Commission concludes otherwise, AIC does not object to Staff's methodology for calculating the balance and embedded cost of preferred stock.

The Commission has considered the record on this matter and concludes that adoption of Staff's position is most appropriate. Earlier in this Order, the Commission determined that using AIC's average capital structure is warranted. Staff's position on this issue is consistent with the use of AIC's average capital structure.

H. Cost of Short-Term Debt, including Cost of Credit Facilities

There are two contested issues regarding the cost of short-term debt: 1) the amount of credit facilities fees to be reflected in the weighted average cost of capital ("WACC"); and 2) the determination of the cost of short-term debt. With regard to the first issue, after adjusting the fees associated with credit facilities that were jointly arranged for AIC and its non-utility affiliates in accordance with Section 9-230 of the Act, Staff determined annual credit facility commitment fees of $5,490,382 for AIC. To calculate AIC's credit facility cost, Staff prorated the costs associated with the June 30, 2009 credit facility using the same proration AIC employed (i.e., 252 days for the credit facility costs the Commission examined in the 2009 rate case and 113 days for the credit facility costs the Commission examined in the 2011 rate case). Finally, Staff divided AIC's total bank commitment fees by total capitalization. Thus, Staff added 14 basis points to AIC's overall cost of capital.

Staff's calculation used the costs for the June 2009 credit facility that the Commission authorized in Docket Nos. 09-0306 et al. (Cons.) and the costs of the September 10, 2010 credit facility that the Commission authorized Docket No. 11-0282. Staff observes that the Commission adopted its adjustment to reduce bank commitment fees associated with the Illinois credit facility, stating:

> The Commission is rightfully concerned that the ratepayers of [AIC] not subsidize the cost of Ameren's borrowing, and therefore, the Commission will adopt Staff's proposal on this issue… Staff postulates that there were no benefits to jointly negotiating that Facility with the Missouri Facility and that the allocation of overall costs to the Illinois Facility was too high. The Commission finds Staff's arguments on this issue convincing, and will adopt Staff's proposed facility fee adjustments for the purpose of this proceeding. (Docket Nos. 09-0306 et al. (Cons.), April 29, 2010 Order at 157-158)

Staff states further that in Docket No. 11-0282, the Commission found that AIC failed to demonstrate that it is certain, or even likely, that the fee rate schedule for the Illinois credit facility would have been exactly the same if it had been negotiated totally independently from the other two credit facilities that Ameren and its subsidiaries entered into during July 2010. (See Docket No. 11-0282, January 10, 2012 Order at 63) Staff urges the Commission to adopt Staff's proposed cost of credit facility fees, as it has done in past AIC rate proceedings.

AIC recognizes that the Commission accepted Staff's adjustment in Docket No. 11-0282. Nevertheless, AIC continues to assert that the adjustment is not warranted. AIC states that it paid an upfront fee equivalent to 66.5 basis points, which it believes is comparable to other Illinois utilities with similar credit ratings. As an example, AIC claims that ComEd paid a fee of 60.5 basis points and Peoples Gas and its affiliates paid fees in an approximate range of 65-75 basis points. Given that Staff's adjustment is intended to remove any financial impacts associated with unregulated affiliates pursuant to Section 9-230, AIC requests that the Commission afford a degree of proportionality and use ComEd's fee equivalent of 60.5 basis points as a proxy in lieu of Staff's proposed adjustment. But in response, Staff argues that AIC has yet to acknowledge the fact that whether AIC's fees are reasonable in comparison to the fees other companies pay to obtain a credit facility is irrelevant because Section 9-230 adjustments are not based on a reasonableness standard. Rather, Staff states that Section 9-230 prohibits incremental costs resulting from non-utility affiliates, regardless of whether a "market-based analysis" suggests those costs are reasonable.

Consistent with its past decision in Docket No. 11-0282, the Commission will adopt Staff's adjustment concerning credit facilities. As previously found by the Commission, AIC has failed to demonstrate that it is certain, or even likely, that the fee rate schedule for the Illinois credit facility would have been exactly the same if it had been negotiated totally independently from the other two credit facilities that Ameren and its subsidiaries entered into during July 2010.

With regard to the second contested issue concerning short-term debt, the cost thereof is only contested to the extent that AIC has no short-term borrowings in a year. In years that AIC has short-term borrowings, Staff recommends that in future formula rate proceedings AIC’s cost of short-term debt should equal the weighted cost of short-term borrowings, as provided in AIC’s Form 10-K, because FERC Form 1 does not separately present short-term debt costs from total debt costs. AIC agreed to use Staff’s proposed cost of short-term debt when it has a short-term debt balance.

Whenever its short-term debt balance is zero, AIC recommends using the cost of short-term borrowings defined under its revolving credit facility. Under its revolving credit facility, the cost of short-term debt is LIBOR plus 205 basis points. AIC proposes this alternative because if it had no short-term borrowings in a year, the short-term debt rate used for ratemaking purposes should not be the cost of short-term debt on Form 10-K, which in that instance would be an Ameren consolidated value, and which might not be appropriate for ratemaking purposes.

In years when the short-term debt balance is zero, Staff argues that the cost of short-term borrowings defined under the revolving credit facility is inappropriate for formula ratemaking since it would not reflect the actual interest costs incurred by AIC for short-term borrowings. Moreover, Staff contends that AIC’s proposal to specify a cost rate for a zero short-term debt balance is meaningless. Staff notes that AIC did not apply any cost rate to its 2010 short-term debt balance of zero. Staff states further that it finds AIC's proposal puzzling because AIC has not described any instance in which a short-term debt cost would be needed if the balance of short-term debt is zero. In Staff’s view, the cost of short-term debt should be zero whenever the short-term debt balance for a given calendar year is zero; and if there is short-term debt outstanding in a year, then the cost of short-term debt calculation should begin with the actual cost for AIC, as set forth in AIC’s Form 10-K. Staff urges the Commission to adopt Staff’s proposed methodology for determining the cost of short-term debt in future formula rate proceedings.

The Commission is puzzled by AIC's seemingly inconsistent positions. Under its own proposed capital structure, where its 2010 short-term debt balance is zero, AIC did not apply any cost rate for short-term debt. But in future formula rate proceedings when the short-term debt balance is zero, AIC recommends using the cost of short-term borrowings defined under its revolving credit facility. The Commission cannot reconcile these conflicting positions. In contrast, Staff proposes a consistent and logical solution of assigning short-term debt a cost of zero whenever the short-term debt balance for a given calendar year is zero. The Commission finds Staff's position reasonable and will adopt it.

I. Other

At pages 39 and 40 of its Initial Brief, Staff recommends several changes to the sources and descriptions provided in AIC Schedule FR D-1 and Apps 12 and 13 to reflect Staff's recommendations regarding the rate of return on rate base. The Commission hereby adopts those changes consistent with the conclusions contained herein. Staff is directed to work with AIC to maintain consistency with AIC's naming conventions and numbering scheme in its formula rate template and supporting workpapers.

IX. COST OF SERVICE

According to AIC, Section 16-108.5 of the Act requires that rate design and cost allocation used to develop rates must be consistent with the participating utility's most recent general rate increase order. AIC proposed a rate design and cost allocation consistent with the Commission's last rate case order issued in Docket Nos. 09-0306 et al. (Cons.), making revisions as necessary in response to Staff concerns to ensure proper calculations were made. AIC and Staff resolved all methodological differences with regard to the statutory requirement by the time of the evidentiary hearing. The Commission approves the use of Staff's proposed Class Revenue Allocation constraint of +/- 50% of the system average rate change for a Rate Zone. Staff's methodology ensures that classes and subclasses do not receive a change that is more than 50% above the change for the rate zone as a whole. The Commission also accepts AIC's proposed modifications to Rate MAP-P tariffs which incorporate Staff's proposed Class Revenue Allocation methodology. No other parties testified on this issue.

X. FORMULA RATE TARIFF

A. Uncontested Issues

1. Uncollectibles Expense - Reconciliation in Rider EUA

Staff witness Hathhorn recommends changes to the formula rate tariff that would essentially mean the formula rate would always reflect zero for the uncollectible expense component in the annual reconciliation, with the reconciliation of uncollectible expense occurring pursuant to the uncollectible expense adjustment rider, Rider EUA. AIC agreed to these revisions, which were reflected in its rebuttal filing. AIC plans for the compliance Rate MAP-P tariff at the conclusion of this proceeding to reflect the agreed-to changes and those ordered by the Commission.

2. Interest Rate Formula for Reconciliation Computation

Staff's direct testimony schedules contained computational errors for the interest rate formula for reconciliation computation. In rebuttal testimony, AIC witness Stafford presented a comparison of Staff's calculation sponsored by Ms. Hathhorn with AIC's Sch FR A-4, as well as proposed revisions to the computation. Staff agreed that the corrections be made. The interest rate to be used in reconciliation filings is contested, and is addressed below in this Order.

3. Period of Time for Compliance Filing

Rate MAP-P includes a provision allowing AIC to file its updated delivery service charges within four business days after the Commission issues its order pertaining to such updates. A period of four business days was selected to allow sufficient time to accommodate potential changes required by the Commission within the formula rate. AIC and Staff agree the period of four business days is reasonable considering the added additional complexity of submitting delivery service tariff filings for three separate rate zones.

4. Rate Case Expense

While IIEC continues to believe that its proposed cap/trigger is appropriate and consistent with the formula rate law it recognizes that the Commission rejected a similar cap in the recently completed ComEd Formula Rate case. Staff notes the Commission's action in the ComEd Formula Rate Case in its Initial Brief. IIEC says the Commission's rejection of IIEC's proposed cap is based on its analysis of recent Commission decisions and case law as well as Section 9-229 of the Act.

In order to minimize the disputed issues in this case, and in consideration of the Commission's analysis of applicable statutory and case law, which specifically requires that the Commission determine the justness and reasonableness of expenses incurred to prepare and litigate a rate case filing, IIEC no longer believes that its cap is absolutely necessary as an additional protection for utility customers. Therefore, IIEC is no longer requesting that its proposed cap/trigger on rate case expense be implemented in this proceeding.

5. Miscellaneous Agreed Tariff Language Revisions

The various agreed-upon changes to the tariff language are listed in AIC Exs. 12.1, 13.1, and 23.1. The tariff revisions necessary for Rider EUA are set forth in AIC Ex. 12.2. Staff also states that in its Initial Brief, it suggested that AIC's submitted tariffs be revised in two instances where AIC could have provided additional detail regarding termination terms and conditions for Rate MAP-P, similar to the level of detail found in ComEd's Delivery Service Pricing and Performance ("DSPP") tariff filing. Staff says AIC witness Mill indicated that AIC's Rate MAP-P compliance tariff would reflect Staff's requested language in both cases. Despite Mr. Mill's statement in rebuttal testimony, Staff says it is not clear from AIC's Initial Brief that the tariff has been or will be revised to reflect this recommendation. According to Staff, AIC states that, “various agreed upon changes to the tariff language are listed in Ameren Exhibits 12.1, 13.1 and 23.1” (Staff Reply Brief at 36, citing AIC Initial Brief at 80-81), but none of these exhibits currently reflects the Staff recommended language on termination terms and conditions. Staff suggests that although this omission may have been unintentional, for the purpose of administrative ease and to avoid any future confusion, Staff would recommend that Ex. 12.1 be revised to reflect this additional language. The Commission concurs that the record should leave no doubt as to the parties' agreement on this issue.

B. Contested Issues

1. Incentive Compensation - Stated Level/Test of Reasonableness

a. IIEC Position

IIEC proposes that a procedural cap be set for incentive compensation expense included in the formula rate. IIEC says the cap acts as a trigger. Under IIEC's proposal, if AIC proposes to include a level of incentive compensation expense in excess of the cap in its formula rate, the Commission would initiate a hearing to determine whether the level of expense requested by AIC was prudent and reasonable. According to IIEC, incentive compensation expense has been one of the more heavily litigated issues in recent AIC rate cases. IIEC states that the Commission has only 45 days in which to review AIC's annual reconciliation filing. IIEC claims that because of the sensitive nature of the incentive compensation expense, it has been separately identified in Section 16-108.5 as a subject of the formula rate. IIEC asserts that recovery of this expense is still subject to the Commission’s overall authority to determine whether a particular expense is prudent and reasonable. IIEC argues that given the sensitivity of this expense, and given the fact that the Commission has only 45 days in which to consider whether it will conduct a hearing on the utility’s annual rate filing, it would be important for the Commission to advise the utility in advance of the pre-determined levels of expense that would cause the Commission to conduct a hearing on the prudence and reasonableness of those expenses.

IIEC recommends the Commission establish a trigger or a cap on the level of incentive compensation expense included in AIC's formula rate. Specifically, IIEC recommends that AIC's incentive compensation expense be limited to the average of the incentive compensation expense approved for AIC in its last three fully litigated electric rate cases. To the extent AIC's incentive compensation expense exceeds that amount, IIEC suggests that the Commission announce to AIC that it will conduct a hearing on the prudence and reasonableness of that expense.

According to IIEC, AIC argues that the cap proposal is a recommendation that the utility recover something other than its actual cost. IIEC says AIC's argument appears to be based on the assumption that the formula rate law allows the utility to recover all its actual costs. IIEC contends that the utility is allowed to recover only actual costs that are prudently incurred and reasonable in amount. IIEC's cap is intended to act as a procedural trigger that would require a hearing on the prudence and reasonableness of expenses that exceed the cap. IIEC says it would not prevent recovery of any prudent and reasonable delivery service cost.

IIEC contends that its proposed cap also is not intended to prevent Commission review of any incentive compensation expense below the cap level. IIEC says those costs must also be for prudent and reasonable; therefore, the cap would not permit recovery of incentive compensation expense that does not satisfy the statutory tests: prudently incurred and reasonable in amount.

AIC argues that there is no lack of scrutiny of incentive compensation expenses, or any other expense, under the formula rate law and that there is no need for "aggressive management" of this expense. IIEC disagrees. IIEC states that the formula rate law provides for annual formula rate filings/updates/reconciliations by the utility based on actual costs shown on the relevant FERC Form 1. According to IIEC, the statute does not require the utility to show that costs recorded on its FERC Form 1 have been prudently and reasonably incurred, only to update its formula rate inputs based on that form. IIEC says the Commission has only 45 days to determine if it will conduct a hearing on the updated data. IIEC asserts that the Commission cannot benefit from the input of the Commission Staff or any customer, since no potential party has any right to discovery or other participation. IIEC also claims that the formula rate law effectively shifts the burden of going forward on issues of prudence and reasonableness of utility expenses and costs recorded in FERC Form 1. Under such a regime, IIEC believes it is reasonable to put in place a mechanism, like IIEC's proposed cap, that gives utilities an incentive to aggressively manage these costs.

IIEC says AIC argues that IIEC's intended procedural cap on incentive compensation violates the formula rate statute. IIEC states that Section 16-108.5(c)(4)(A) allows a utility to recover incentive compensation that is based on the achievement of certain operational metrics. According to IIEC, AIC ignores or overlooks provisions of the same section limiting recovery of incentive compensation costs to actual delivery service costs that are prudently and reasonably incurred. IIEC argues that because its proposed cap operates as a trigger for a hearing to determine the prudence and reasonableness of reported incentive compensation expense, it is fully consistent with the formula rate law.

IIEC believes that Staff misunderstands IIEC's proposal. Staff asserts that IIEC's cap would substitute an assumed amount of incentive compensation expense for AIC's actual cost and presume that amount to be prudent and reasonable. IIEC insists it is proposing a procedural cap, not an absolute ceiling on, or even a floor for, incentive compensation recovery. IIEC says that although its proposed cap would act as a trigger for a hearing on the main criteria for cost recovery (prudence and reasonableness), Staff suggests that it agrees that IIEC's proposal is unnecessary. IIEC maintains that its proposed cap is needed.

b. AIC Position

In AIC's view, the General Assembly makes clear in Section 16-108.5 of the Act that the formula rate process would provide for the recovery of the utility's actual costs and that the actual cost data was to come from the utility's most recently filed annual FERC Form 1. AIC argues that contrary to this plain statutory language, IIEC witness Gorman recommends the Commission establish a "stated level" of rate case expenses, affiliate service charge expenses, and incentive compensation. Under IIEC's proposal, if AIC's actual expense equals or is less than the "ceiling," then that amount of the expense is automatically included in Rate MAP-P. If AIC's actual level of that expense is greater than the stated level, then under IIEC's proposal AIC can choose to include only the stated level in Rate MAP-P or the Commission can initiate an investigation to determine the reasonableness of the higher actual level.

According to AIC, Mr. Gorman recommends that something other than the actual cost as reported on FERC Form 1 be used to set the Rate MAP-P revenue requirement. AIC asserts that Mr. Gorman's proposal appears to be simply a way to reduce recovery by capping it at some arbitrary level. AIC says Mr. Gorman's proposal assumes his "stated level" is reasonable. AIC claims Mr. Gorman's proposal would, instead, substitute an assumed amount, which is presumed to be prudent and reasonable and forgo analysis of the actual amount for the year. In AIC's view, it is contrary to the clear intent of the General Assembly.

AIC contends that the Commission's authority to determine the reasonableness and prudence of expenditures, and to disallow recovery if they are unreasonable or imprudent, provides a very strong incentive for a utility to manage its costs. AIC believes that establishing an arbitrary, rebuttable presumption that expenditures in excess of certain levels are unreasonable establishes an incentive to focus solely on cost recovery, instead of what is reasonably necessary to provide safe and reliable utility service. AIC suggests that capping recovery of lawful expenses is not in the customers' best long-term interest. AIC states that denying recovery of lawful expenses can lead to very negative outcomes such as weakened credit ratings, increased costs of financing, and customers will ultimately pay the increased financing costs.

Mr. Gorman appears to contend that the Commission lacks a "procedural mechanism" to determine whether a utility must show its costs are prudent and reasonable. According to AIC, the law makes it clear that in formula rate reconciliations, the Commission can review the prudency and reasonableness of AIC's actual costs in the reconciliation proceeding. AIC insists the "procedural mechanism" already exists in the formula rate reconciliation process. AIC also notes that Staff agrees Mr. Gorman's recommendation should be rejected because of potential practical difficulties in implementation and because it is inconsistent with the Act.

AIC states that for the incentive compensation expense "ceiling," Mr. Gorman proposes that a cap be set at the average of the Commission-approved levels of incentive compensation expense in AIC's last three rate cases. AIC asserts that Mr. Gorman fails to provide the basis for his proposed calculation of the incentive compensation expense cap, explain why the stated level of that expense should be determined differently than the stated levels for rate case expense and affiliate service charges expense, or explain why an average of the approved-level of the expense from AIC's last three rate cases represents a just and reasonable level of the expense in all formula rates going forward. AIC also complains that Mr. Gorman also fails to explain whether the three rate cases he mentions include gas service incentive compensation amounts.

In AIC's view, the use of the prior three electric rate cases in which an order was entered is not appropriate due to the significant evolution of AIC’s incentive compensation program in that time, such that the historical level of incentive compensation expense approved by the Commission does not have any relationship to AIC's current level of incentive compensation expense. AIC states that the last three electric rate cases in which a Commission order was entered were Docket Nos. 06-0070 et al. (Cons.), Docket Nos. 07-0585 et al. (Cons.) and Docket Nos. 09-0306 et al. (Cons.). AIC says that in Docket Nos. 06-0070 et al. (Cons.), the Commission denied AIC all recovery of incentive compensation expense due to the presence of a "financial trigger." Subsequently, in 2008, AIC claims it modified its incentive compensation plans to remove the financial triggers and emphasize operational "key performance indicators" ("KPIs") with customer benefits. AIC states that the Commission in Docket Nos. 07-0585 et al. (Cons.) and Docket Nos. 09-0306 et al. (Cons.) considered the level of AIC's incentive compensation expense in conjunction with incentive plans that had been significantly changed. AIC insists the Commission's average approved level of expense in those cases is not an appropriate basis for comparison to AIC's incentive compensation costs included in its formula rates.

AIC also argues that Section 16-108.5 of the Act expressly permits the recovery of incentive compensation expense that is based on the achievement of operational metrics, including metrics related to budget controls, outage duration and frequency, safety, customer service, efficiency and productivity, and environmental compliance. AIC contends that the Act does not contain any limitation, in the manner Mr. Gorman suggests, on recovery of incentive compensation expense based on achievement of those statutory metrics. AIC urges the Commission to reject Mr. Gorman’s proposal.

According to AIC, IIEC ignores that Section 16-108.5(c) does not specify a dollar limit; instead it expressly allows a utility to recover actual costs. AIC claims that IIEC disregards the fundamental principle that the Commission has only those powers granted to it by the legislature. AIC claims that while IIEC might wish that the expenses subject to formula rate review could be set at some arbitrary threshold, the EIMA does not provide for this. AIC says the General Assembly intended the formula rate process to provide for the recovery of the utility’s actual costs and that the actual cost data was to come from the utility’s most recently filed annual FERC Form 1. AIC believes that establishing an arbitrary presumption that expenditures in excess of certain levels is unreasonable and contrary to law.

AIC also indicates that Section 16-108.5(c)(1) of the Act states that the sole fact that a cost differs from that incurred in a prior calendar year or that an investment is different from that made in a prior calendar year shall not imply the imprudence or unreasonableness of that cost or investment. In AIC's view, the General Assembly made clear it understood that expenses could vary from year to year, and that any variation did not imply an expense somehow became unreasonable simply because it changed, or rose above some arbitrary threshold.

c. Staff Position

Staff disagrees with Mr. Gorman's proposal. Based on Staff's understanding of Section 16-108.5(c) of the Act, the statute permits the recovery of incentive compensation expense in the formula rates, subject to a determination of prudence and reasonableness consistent with Commission practice and law, to the extent that such incentive compensation expense is based on the achievement of operational metrics, including metrics related to budget controls, outage duration and frequency, safety, customer service efficiency and productivity, and environmental compliance. Staff states that incentive compensation that is based on net income or an affiliate's earnings per share shall not be recoverable under the performance-based formula rate. Staff also says the Act does not specify a dollar limit, instead it provides for the actual amount to be considered for prudence and reasonableness, within the context of the statute. Staff states that Mr. Gorman's proposal would, instead, substitute an assumed amount which is presumed to be prudent and reasonable and forego analysis of the actual amount for the year.

d. Commission Conclusion

IIEC proposes what it describes as a procedural cap to be set for incentive compensation expense included in the performance based formula rate. Under IIEC's proposal, if AIC proposes to include a level of incentive compensation expense in excess of the cap in its formula rate, the Commission would initiate a hearing to determine whether the level of expense requested by AIC was prudent and reasonable. IIEC expresses concern that the Commission has only 45 days in which to review AIC's annual reconciliation filing. IIEC suggests the Commission advise the utility in advance of the pre-determined levels of expense that would cause the Commission to conduct a hearing on the prudence and reasonableness of those expenses. AIC and Staff both object to IIEC's proposal. Among other things, they believe it is unnecessary and is inconsistent with the Act.

The Commission first notes that the ratemaking treatment of incentive compensation has been the subject of extensive litigation in recent years. This may be the reason it was one of the types of expenses that was explicitly addressed when the General Assembly passed Public Acts 97-0616 and 97-0646. Section 16.108.5(c) of the Act permits the recovery of those actual incentive compensation expenses which are related to certain operational metrics, are reasonable in amount, and are prudently incurred.

Given the statutory framework relating to recovery of incentive compensation expenses and the performance based formula rate mechanism, the Commission does not find IIEC's proposal necessary or appropriate. If adopted, such a proposal could result in unnecessary investigations or alternatively, provide a false sense of security that certain incentive compensation expenses are reasonable and prudent because they do not exceed the cap or trigger level.

2. Incentive Compensation - Metrics/Requirements

a. IIEC Position

IIEC proposes a limitation on incentive compensation expense that would be included in the formula rate. Under IIEC's proposal, incentive compensation would be recoverable under the formula rate only if the reliability metrics for AIC are satisfactorily met. IIEC suggests the minimum operational metric standards AIC must meet should be the standards described in Section 16-108.5(f) of the Act. These standards were the subject of Docket No. 12-0089. IIEC states that Section 16-108.5 includes language which provides that AIC’s formula rate permit and set forth protocols for recovery of incentive compensation based on the achievement of operational metrics.

IIEC believes that to be included in the formula rate, incentive compensation expense should be structured so that achieving or exceeding the metric thresholds is a condition of its inclusion to the extent it is otherwise recoverable. IIEC recommends that failure to achieve the metrics would mean that no incentive compensation expense would be included in the formula rate. IIEC asserts that failure to meet the operational metrics that form the basis of incentive compensation recovery is an indicator the expenses for rewarding employees for performance are not prudent or reasonable and that inclusion of those expenses in the formula rate would result in a rate that is not just and reasonable.

In order to accomplish this goal, IIEC says the Commission should require that AIC include with its annual filing, the information necessary to allow the Commission to determine whether or not AIC has achieved the metrics approved by the Commission. According to IIEC, both Staff and AIC overlook the fact that the Commission is required to determine whether incentive compensation costs incurred by AIC are prudent and reasonable. IIEC says the Commission’s determination of the prudence and reasonableness of AIC’s incentive compensation costs can consider whether the costs are achieving anticipated system reliability, safety and efficiency gains -- areas measured by the metrics described in Section 16-108.5(f). IIEC asserts that Section 16-108.5(c)(4)(A) contemplates that recovery of incentive compensation expense will be based on the achievement of operational metrics described in that Section. IIEC insists that AIC's recovery of incentive compensation can be conditioned on achievement of the metrics identified by IIEC.

IIEC states that AIC argues that IIEC's proposal is simplistic in that it ties AIC's recovery of incentive compensation expense to achievement of a limited number of performance metrics. IIEC says it has no objection to broadening the spectrum of metrics that must be met as a condition of recovering incentive compensation through the formula rate.

b. AIC Position

AIC asserts that IIEC's proposal should be rejected because there is no statutory basis for the recommendation and the proposal ignores AIC's broad range of KPIs and their customer benefits. AIC indicates that Section 16-108.5(c)(4)(A) of the Act expressly permits recovery of incentive compensation expense that is based on the achievement of operational metrics, including metrics related to budget controls, outage duration and frequency, safety, customer service, efficiency and productivity, and environmental compliance. AIC contends that no provision is made in the statute for the trigger mechanism IIEC describes. AIC further argues that these incentive compensation metrics are not the same as the metrics AIC must meet under in Section 16-108.5(f) of the Act. AIC says penalties for failure to achieve the metric goals in Section 16-108.5(f) are set out in Section 16-108.5(f-5). AIC insists that these penalties do not include a disallowance of incentive compensation expense for failure to achieve the metrics. AIC notes that Staff agrees that Section 16-108.5 does not impose this requirement for recovery of incentive compensation expense.

In AIC's view, Mr. Gorman's recommendation is a simplistic attempt to link recovery of all AIC incentive compensation expense to AIC's achievement of a limited number of separate performance metrics. AIC claims its incentive plans cover a far wider range of operational areas than the metrics to which Mr. Gorman refers. AIC states that while it is true that some KPIs are based on system average interruption frequency index or customer average interruption duration index performance, many other KPIs relate to operational and other areas that have no connection to the metrics to which Mr. Gorman refers. AIC contends these KPIs also have operational and customer benefits. AIC claims it has safety related KPIs that are not included in the metrics to which Mr. Gorman refers. AIC asserts that Mr. Gorman's proposal would potentially deny AIC the opportunity to recover the cost of safety KPIs despite their clear operational and customer benefits, for failure to meet unrelated statutory goals. AIC also claims its incentive plans establish KPIs for both company and individual performance. AIC says these KPIs may continue to produce operational and customer benefits even if, hypothetically, AIC did not meet the performance metric goals in Section 16-108.5(f) on a company-wide basis. AIC insists that its incentive plans cover a far wider range of metrics (KPIs) than the metrics in Section 16-108.5(f) of the Act. AIC believes a proposal to condition recovery of incentive compensation expense on achievement of the statutory metrics ignores AIC's broad range of KPIs and their customer benefits.

c. Staff Position

IIEC witness Gorman also recommends that the Commission impose a condition whereby AIC would have to satisfy its performance metrics and reliability standards in order to recover incentive compensation expense in the formula rates. Staff does not oppose the idea that AIC could incorporate some additional metrics related to Section 16-108.5(f) into its incentive compensation plans prospectively; however, Staff does not understand Section 16-108.5 to impose this requirement for recovery of incentive compensation expense in the formula rates in the manner Mr. Gorman proposes.

d. Commission Conclusion

IIEC proposes that in order for incentive compensation expenses to be recoverable under the formula rate, the reliability metrics for AIC must be satisfactorily met. IIEC suggests the minimum operational metric standards AIC must meet should be the standards described in Section 16-108.5(f) of the Act. The IIEC proposal is opposed by AIC and Staff. Among other things, they claim that the proposal is not contemplated under the language in the Act.

As discussed in the immediately preceding section of this Order, Section 16-108.5(c) of the Act lays out the requirements that must met be for a participating utility to recover incentive compensation expenses from customers. Section 16-108.5(f) of the Act addresses the multi-year metrics plan to improve utility performance on certain parameters. Section 16-108.5(f-5) of the Act addresses the financial penalties associated with failing to meet the metrics addressed in Section 16-108.5(f-5).

The Commission understands that Section 16-108.5(c) requires that incentive compensation expenses must be based on the operational achievement of certain operational metrics, and not other financial metrics, to be recoverable under the performance based formula rate. Reading the statute in its entirety, it does not appear that the General Assembly contemplated that recovery of incentive compensation expenses under the performance based formula is dependent on meeting the metrics specified in Section 16-108.5(f). Therefore, IIEC's proposal will not be adopted.

On the other hand, if a utility fails to meet some or all of the metrics specified in Section 16-108.5(f), one might question the level of prudent or reasonable incentive compensation expenses that the utility be allowed to recover under performance based formula rate. Of course, that is a question that the Commission cannot and will not address in this Order.

3. Affiliate Service Charges

a. IIEC Position

IIEC recommends that the amount of affiliate service charges expense that AIC proposes for inclusion in its formula rate in this case, $124 million, be used as the cap or trigger on AIC's formula rate on a going-forward basis. IIEC states that under the formula rate approach, these expenses and charges will not receive regulatory scrutiny as in a traditional rate case, because they may simply be plugged into the formula rate at the recorded value contained in FERC Form 1. IIEC believes that including a cap or trigger in the formula rate for this expense would ensure customers that they pay no more than a reasonable level of this expense. Under IIEC's proposal, if the $124 million is below AIC's actual affiliate service charge expense, then AIC would have the ability to present evidence in the context of the hearing that would be triggered to demonstrate the reasonableness of the expense level it proposed to recover. IIEC says if AIC's expense level does not exceed the $124 million amount, the Commission would still have the authority to examine the prudence and reasonableness of the expense level proposed by AIC, if it were inclined to do so. IIEC claims that including a cap will ensure that the costs recovered by AIC in the formula rate are prudent and reasonable and encourage AIC to actively manage that expense.

According to IIEC, both Staff and AIC suggest that IIEC's proposal does not comport with Section 16-108.5. IIEC asserts that neither AIC nor Staff explain how or why a procedural cap on affiliate service charges, operating as a trigger for a hearing on the prudence and reasonableness of the costs, is inconsistent with the formula rate law or is not within the Commission's authority to issue rules for the administration of the formula rate law. IIEC says Staff and AIC's arguments are based largely on the premise that IIEC's proposed cap is an absolute cap. IIEC contends that the proposed cap is a procedural device to trigger scrutiny of proposed costs.

Staff also agrees with AIC's argument that IIEC's proposal is unnecessary given the formula rate reconciliation process. IIEC maintains that the time constraints on the Commission's review of AIC's annual formula rate filing, which includes the reconciliation, justify a procedural prompt to signal a need for closer scrutiny of certain costs. In IIEC's view, the statutory period for reconciliation under Section 16-108.5 is simply not ample time to assess costs. IIEC also states that the Commission's decision on conducting a hearing must be made without the benefit of discovery by the Staff or customers. IIEC believes a cap to trigger a hearing on the prudence and reasonableness of AIC's affiliate costs above the cap would provide customers with additional protection under the process described under Section 16-108.5(d). IIEC also claims a cap would provide AIC with the incentive to include in FERC Form 1 only those costs and expenses that are prudently incurred ad reasonable in amount.

IIEC states that while the Commission declined to adopt a similar cap/trigger mechanism in the recently concluded ComEd formula rate case, the Commission found merit in the concerns prompting IIEC's proposal. IIEC says if the Commission adopts the same approach in this case, as it did in the ComEd formula rate case, IIEC accepts that there is no need to adopt its cap on affiliate charges. However, IIEC still considers a procedural cap/trigger to be the superior approach.

b. AIC Position

AIC understands Mr. Gorman to recommend that the Commission impose a "stated level" of affiliate service charges, although it is not clear what that stated amount is. AIC says at one point he recommends $124 million, which is the amount on AIC's 2010 FERC Form 1. According to AIC, IIEC alleges these expenses will not receive regulatory scrutiny as in a traditional rate case, thus the proposed cap will ensure customers pay no more than a reasonable level for this expense. (AIC Reply Brief at 58-59) AIC believes its proposed level of affiliate service charges expenses is appropriate in this proceeding. AIC indicates that Mr. Gorman also states that AIC should identify all affiliate service charges included in its last rate order to use as this stated value. In AIC's view, his recommendation is unclear. AIC insists that in any event, that figure should not serve as a cap on the level of the expense in future formula rates. AIC contends that Mr. Gorman's proposal is at odds with the intent of the General Assembly that the formula rate process would provide for the recovery of the utility's actual cost and that the actual cost data was to come from the utility's most recently filed annual FERC Form 1.

c. Staff Position

Staff notes that Mr. Gorman asserted that these affiliate service charges will not receive regulatory scrutiny within a formula rate case; therefore, he proposed to limit them to a stated value to ensure that customers will pay no more than a reasonable level for this expense. Mr. Gorman recommends going forward that the Commission use a "stated level" equal to $124 million - the amount of affiliate service charges expense included in the instant proceeding, in lieu of actual expense. Staff says he references this amount to the formula rate filing (Sch. FR C-13 A, Sch. 13 B and Sch. 13 C). Staff indicates it was unable to locate these schedules or the $124 million to which Mr. Gorman refers.

Staff disagrees with Mr. Gorman's proposal because Staff believes it does not comport with Section 16-108.5 of the Act. Staff understands that Section 16-108.5 permits recovery of affiliate service charge expense in the formula rates, subject to a determination of prudence and reasonableness, consistent with Commission practice and law. Staff does not support the substitution of actual expense amounts with a stated amount in future proceedings.

d. Commission Conclusion

As the Commission understands it, IIEC's proposal here is similar to the procedural cap or trigger it proposed for incentive compensation expense which was discussed earlier in this Order. Under IIEC's proposal, if AIC's actual affiliate service charge expense is greater than $124 million, then a hearing would be triggered and AIC would have the ability to present evidence to demonstrate the reasonableness of the expense level it proposed to recover. IIEC says if AIC's expense level does not exceed the $124 million amount, the Commission would still have the authority to examine the prudence and reasonableness of the expense level proposed by AIC, if it were inclined to do so. IIEC's proposal is opposed by both AIC and Staff who argue, among other things, that it is unnecessary and inconsistent with the Act.

As noted above, IIEC's proposal here is similar to its proposal regarding incentive compensation expenses, which the Commission has rejected. The Commission again concludes that, given the statutory framework relating to recovery of affiliated interest charge expenses and the performance based formula rate mechanism, IIEC's proposal is not necessary or appropriate. If adopted, such a proposal could result in unnecessary investigations or alternatively, provide a false sense of security that certain affiliate service charge expenses are reasonable and prudent because they do not exceed the cap level.

4. Schedules to be Included in Rate MAP-P/Tariff Complexity

a. AIC Position

AIC proposes to make part of the published Rate MAP-P tariff the schedules that include the various formulae used in determining the revenue requirement and the resulting charges. AIC believes this is consistent with the Act's intent that formula rates specify the cost components that form the basis of the rate charged to customers with sufficient specificity to operate in a standardized manner and be updated annually with transparent information. AIC notes that Staff and IIEC oppose their inclusion, arguing the Commission ruled in the ComEd case, Docket No. 11-0271, a more limited version is appropriate, and contending the subject tariff is too complex and confusing.

AIC maintains the information and formulas are needed for a complete understanding of the tariff and claims no party has argued differently. AIC also asserts that the Commission's practice with riders has been to include the formulas. AIC contends that Rate MAP-P does not become less complicated if the formula schedules are not attached to the actual tariff. AIC argues that the Schedules (formula) should be readily available to understand how the rate works.

According to AIC, the revisions to the Act intended to create a transparent formula ratemaking process; thus, including the formulae is consistent with that intent. AIC also asserts that if a person wants to disregard the schedules, that is a choice he can make; but insists there is no burden if the schedules remain. AIC believes that members of the energy community prefer more information, not less.

In response to the references to Docket No. 11-0721, AIC says the Commission is being presented with additional facts regarding this issue in this docket by which to conclude the added formulae are not an impediment but, indeed, useful information. AIC also asserts that IIEC incorrectly describes the tariff as including workpapers, claiming these "workpapers" are actually schedules that include the formulae explaining how the rate is developed. AIC believes IIEC's contention that most customers would have no need for the formula is without merit. AIC states that while the typical residential customer would have no need for the formula, other customers such as commercial and industrial customers, and retail electric suppliers may find benefits in knowing how the revenue requirement and other charges are being calculated.

AIC says Staff witness McClerren recommends that Rate MAP-P include Schedules FR-A1 and FR-A1 Rec, but that the remaining schedules be part of the filing and not the tariff. AIC claims he offered no independent reasoning but for the Commission's decision in the ComEd case. Similarly, Staff witness Hathhorn on rebuttal made the proposal that the compliance version of Rate MAP-P only include Schedules FR-A1 and FR-A1 Rec, with all other formula rate sheets in Appendix A, and apparently the rate design template sheets in Appendix B of Rate MAP-P being excluded from the tariff. AIC also observes that Ms. Hathhorn recommends the "final template" which is to include all "schedules" be provided to the Manager of Accounting, which AIC is willing to do. AIC questions why, if it is important for Staff to have these schedules, why is it not important for members in the energy community to also be privy to same.

AIC states further that Ms. Hathhorn clarifies how the remaining formula sheets being removed from Appendices A and B of Rate MAP-P should be addressed, stating that the Commission order should be clear that the Commission is adopting as the formula all the schedules that comprise the template. AIC says she references Section 16-108.5(d)(3) of the Act and concludes that the Commission does not have authority to approve any further changes to the formula adopted in this proceeding. AIC agrees that the Commission does not have authority to approve any further changes to the formula adopted in this proceeding. AIC also agrees that filing the template on e-Docket is necessary, should the Commission determine to exclude Appendix A and B rate sheets from the tariff.

According to AIC, IIEC makes claims or allegations not supported in the record. AIC says IIEC argues AIC's proposal would hinder the Commission's exercise of its ratemaking authority. AIC does not believe including the formulas would have any impact on the Commission's ratemaking authority. AIC maintains that the schedules, which are the formula approved by the Commission, serve to develop the revenue requirement and the other rate charges. AIC says all the inputs are approved by the Commission, not AIC.

AIC states that IIEC claims there might be limitations on the Commission's ability to modify cost inputs. AIC asserts that there is no factual basis in the record for this statement. AIC claims it is speculative and wrong. AIC insists that with each formula rate case, the Commission will make the decisions by which to populate the formula rate values. AIC contends there is no chance of limiting the Commission's authority. AIC urges the Commission to disregard this portion of IIEC's position.

b. IIEC Position

IIEC states that the statutory tests for the formula rate are functional ones. According to IIEC, the statute is silent on the level of detail necessary or appropriate for an implementing tariff. IIEC states that the Commission is the regulatory body charged by statute with implementing the formula rate regime, and it is the Commission that is authorized to determine how much detail is required to be sufficient for those purposes.

IIEC believes AIC's proposed tariff is an excessively detailed tariff and is modeled on ComEd's proposed formula rate. IIEC says that while AIC may be familiar with and comfortable with its tariff, the Commission and retail customers in AIC's service territory may view the proposed tariff as a novel mechanism warranting close examination. IIEC asserts that AIC's preference for a workpaper level of detail in the formula rate does not make such detail either a statutory requirement or an appropriate feature under Article IX of the Act.

It is IIEC's view that AIC's proposed Rate MAP-P is unduly complex and more specific than necessary in order to implement the statutory requirements. IIEC states that currently Rate MAP-P consists of 9 pages plus 2 indices, A and B, consisting of 48 pages and 26 pages respectively. In total, Rate MAP-P consists of 83 pages that reflect a detailed revenue requirement determination method, detailed formula spreadsheets, and spreadsheets for other information related to financial cost indicators and billing delivery units. IIEC asserts that simplicity and understandability are fundamental attributes of sound rate structures. IIEC argues that the level of detail included in Rate MAP-P is far beyond that which is necessary to operate in a standardized matter as required by Section 16-108.5 of the Act.

According to IIEC, the Commission has already expressed its desire to have formula rates be understandable. IIEC says that in Docket No. 11-0721, the Commission adopted IIEC's recommendation to simplify ComEd's formula rate. IIEC asserts that the Commission's decision in the ComEd docket is consistent with prior Commission decisions on the importance of the understandability of utility tariffs.

IIEC contends that AIC proposes to incorporate in its tariffs the type of computation detail that is usually the center of the Commission's regulatory review of proposed revenue and cost bases for proposed rates. IIEC insists the form of the tariff that AIC proposes could hinder or needlessly complicate the Commission's exercise of its ratemaking authority and obligation for Article IX review under the Act. IIEC suggests the Commission would likely have to make numerous tedious tariff revisions for every determination of prudent and reasonable costs or capital structure, on a different record that varies from previous cost inputs or calculations on FERC Form 1 data.

IIEC also claims there might be limitations on the Commission's ability to modify cost inputs if the tariff is interpreted as a constraint on how the Commission determines whether a cost is prudent, or just and reasonable, and how to reflect that in the formula rate calculations. According to IIEC, Section 16-108.5 explicitly directs the Commission to continue its scrutiny of proposed costs and rates in accordance with existing Article IX of the Act, relevant law, and the Commission's customary practices, with very limited exceptions. IIEC believes these tasks will be significantly more difficult if the Commission's modifications of proposed cost inputs require the Commission to search for, change, and verify all tariff spreadsheet entries associated with each Commission determination or modification. IIEC contends that customers participating in formula rate proceedings face equally daunting requirements for objections to proposed costs and revenue requirement computations.

IIEC contends that approval of AIC's proposal to include new schedules and appendices of workpaper details in Rate MAP-P sets the stage for utility arguments to try to immunize tariff cost inputs from meaningful examination, because particularly described cost elements or computations are incorporated in detailed spreadsheets of the tariff. IIEC asserts that AIC's proposed tariff is impossibly complicated, thus, it is not understandable to or accessible by AIC customers who are directly affected by it. Under such circumstances, IIEC believes it does not achieve the transparency required by the new statutory provisions.

Even with the detail and complexity of Rate MAP-P as proposed by AIC, IIEC argues the tariff still lacks the link between the source data in AIC's FERC Form 1 and the revenue requirement formula that comprise the formula rates. IIEC says AIC's Rate MAP-P requires extensive workpapers, nearly 190 pages, to define the tariff formula rate cost inputs. IIEC claims that proposed Rate MAP-P does not allow computation of AIC's revenue requirement directly from FERC Form 1, without using spreadsheets, forms and other computational devices, as well as additional data that are not included in the tariff itself. IIEC asserts that the tariff cannot be updated with transparent cost information any more than a less complicated, more comprehensible tariff. In IIEC's view, a more understandable tariff that shows the formula revenue requirement determination using the major elements of the formula rate, at a level of detail that satisfies the statute, is possible. IIEC has proposed that the Commission exclude Appendices A and B from the tariff and adopt the nine tariff pages that AIC currently lists for Rate MAP-P itself.

IIEC contends that the pages that it recommends be included in the tariff will meet the statutory requirements and better serve the customary purposes of tariffs. In addition, IIEC says the simplified tariff can be supplemented by Commission rules that would govern the formula rate process. IIEC suggests the rules could incorporate the remaining AIC schedules and/or workpapers, as part of standard filing requirements for formula rates. IIEC suggests that AIC's proposed tariff, Appendices, and supporting workpapers, would retain the function documents have in the Commission's customary Article IX reviews of proposed rates. IIEC says the Commission would not be unnecessarily limited in its proper and decisive role in reviewing the prudence and reasonableness of formula rate cost inputs. According to IIEC, because non-tariffed spreadsheets and data are required, even with AIC's proposed more detailed and complex tariff, standardization would not be significantly diminished. IIEC suggests that transparency and understandability of the tariff would be significantly enhanced.

IIEC recommends that what are now Appendices A and B to Rate MAP-P be filed with the Commission for review. IIEC suggests that the Commission should consider the information contained in these two appendices to be part of the standard filing requirements for AIC's formula rate, similar to the standard filing requirements described in Parts 285 and 286 of the Commission's rules. According to AIC, Parts 285 and 286 filings are not made a part of the utility's tariff, even though information from those filings may be reflected in the rates or charges approved by the Commission. IIEC says there may be a need to make the information contained in Appendices A and B a part of the utility's standard formula rate filing, on a going-forward basis; there is no need to make them a part of the tariff itself.

IIEC states that while AIC argues that the information and formulas contained in the hundreds of pages of schedules is needed for a complete understanding of the tariff, (IIEC Reply Brief at 44, citing AIC Initial Brief at 88), its rate design witness, Mr. Mill, has testified that whether or not the schedules are included in rate MAP-P is of "little consequence" to AIC. (Id, citing AIC Ex. 22.0 at 6:112-113). IIEC insists that AIC cannot have it both ways. It cannot argue on one hand that the schedules are needed for complete understanding of the tariff while its expert witness on the subject testifies that including the schedules are of little consequence.

According to IIEC, AIC purports to speak on behalf of customers and stakeholders in recommending the inclusion of the schedules in the tariff. IIEC states that two large and sophisticated customer groups, IIEC and the Commercial Group, as well as Staff support a simpler formula rate tariff. IIEC says no customer group has opposed the simpler version of the tariff. IIEC claims the simplified version of the tariff still contains the necessary elements of the formula for determining the AIC revenue requirement that customer charges will be based on, without the extraneous and confusing schedules.

IIEC asserts that while AIC argues that rate MAP-P is no less complicated if the subject schedules are excluded, it does not explain why this is so. IIEC claims AIC's argument is also contradicted by the Commission's conclusion in Docket No. 11-0721 that these types of additional schedules did, in fact, make the tariff more complex. IIEC states that AIC argues that because the formula rate law intended a transparent formula ratemaking process, inclusion of the hundreds of pages of schedules and multiple formulae, is consistent with that intent. IIEC claims the testimony in this case demonstrates that the tariff does not add to transparency, and in fact, has the opposite effect. According to IIEC, AIC argues that the schedules should be included with the tariff because they can easily be disregarded by those not interested in the detail. IIEC believes that if the schedules can be disregarded, they apparently are not necessary for a complete understanding of the tariff. IIEC says AIC's argument also suggests that an abbreviated version of the tariff will be understood without the addition of dozens of pages of schedules and formulae.

AIC attempts to distinguish the decision on the tariff complexity issue in Docket No. 11-0721 from this case by arguing that it has presented additional facts in this case that were not present in the ComEd case. AIC contends that AIC has not identified exactly what those additional facts are. IIEC also notes that AIC's own rate expert, Mr. Mill, has confirmed that Ameren's rate MAP-P was modeled on ComEd's tariff. IIEC says Mr. Mill also testified that adopting comparable rate designs for ComEd and AIC would facilitate a more efficient review process. IIEC contends that while AIC argues in its Initial Brief for a tariff distinct from the approved ComEd tariff, the testimony of its witnesses supports adoption of a formula rate tariff like ComEd's. IIEC believes the tariffs should be made similar.

IIEC states that AIC argues that it is important for all members of the energy community to have access to the dozens of pages of schedules and formulae in its proposed tariff -- even though AIC has suggested most can be ignored by customers. IIEC maintains there is no reason why these schedules and formulae cannot be made part of standard filing requirements for each utility formula rate filing, as the Commission directed in Docket No. 11-0721. In IIEC's view, there is no need to include these schedules in the formula rate tariff itself to provide customers access to that detailed information. IIEC disagrees with the Staff's recommendation that the Commission should require a filing and make clear that it is adopting "as the formula," all of the subject schedules. IIEC asserts that contrary to Staff's position in Staff's Initial Brief, Staff witness Hathhorn explained on cross-examination that she intended her recommendation (however worded) "to be consistent with what the Commission ordered in the Commonwealth Edison case, Docket 11-0721." (IIEC Reply Brief at 47, citing Tr. at 237-238). IIEC contends that Docket No. 11-0721 requires the subject schedules be made a part of the utility filing, not adopted as the formula.

IIEC also disputes the reason given in Staff's Initial Brief for its recommendation to adopt the schedules as the formula. Staff argues that the Commission does not have the authority to approve changes to the formula rate in subsequent reconciliation proceeding. IIEC asserts that Section 16-108.5(d)(3) does prevent changes to the structure or protocols of the performance-based formula rate approved pursuant to subsection (c). According to IIEC, this subsection prevents changes to the formula rate itself in the context of an annual formula rate filing made under subsection (d) of Section 16-108.5. IIEC insists that this section does not, however, prevent the Commission's modification of the information and schedules, etc. that it requires the utility to file as a supplement to the formula rate. IIEC contends that the Commission is authorized to make changes to the formula rate itself, but under distinct provisions of the Act. IIEC indicates that Section 16-108.5(c) states in part:

> Subsequent changes to the performance-based formula rate structure or protocol shall be made as set forth in Section 9-201 of this Act, but nothing in this subsection (c) is intended to limit the Commission's authority under Article IX and other provisions of this Act to initiate an investigation of a participating utility's performance-based formula rate tariff, provided that

> any such changes shall be consistent with paragraphs (1) through (6) of subsection (c). Any changes ordered by the Commission shall be made at the same time new rates take effect following the Commission's next order pursuant to subsection (d) of this section, provided the new rates take effect no less than 30 days after the date on which the Commission issues an Order adopting the change.

IIEC contends that the Commission has ample authority to make changes to the formula rate, even under what it views as Staff's incorrect interpretation of Section 16-108.5(d)(3). IIEC concludes that the Commission does not need to make the schedules a part of the approved formula because it cannot make changes to the formula rate in a reconciliation proceeding.

c. Staff Position

Staff recommends the Commission adopt the same approach with AIC that it used in the ComEd case. Specifically, Staff believes Rate MAP-P should include Schedules FR-A1 and FR-A1 Rec. Staff states that the remaining schedules may be part of a filing but they should not be part of the tariff. Staff says this would maintain consistency between AIC's formula rate and ComEd's formula rate. Staff contends that both AIC and the Commission recognize the importance of consistency between the two formula rates.

Staff states that the Commission indicated it will initiate a rulemaking to create a systematic approach governing the formula rate process. Staff says such a rule would apply to both ComEd and AIC and assumes consistency between the two formula rates. According to Staff, following the Commission's approach from the ComEd Order would maintain this consistency.

Staff recommends that the Commission should be clear in its Order that it is adopting as the formula all the schedules that comprise the template pursuant to Section 16-108.5(d)(3) of the Act. Staff concludes that the Commission does not have the authority to approve any further changes to the formula adopted in this proceeding. Staff also recommended that the Commission order AIC to file on e-Docket, with a copy to the Manager of Accounting of the Commission, the final template approved by the Commission that consists of all schedules comprising the formula by the time rates resulting from this order are effective.

d. The Commercial Group Position

The Commercial Group suggests the Commission should set a rate formula that ratepayers have a better chance understanding than the 83-page rate formula submitted by AIC. The Commercial Group notes that in this proceeding, IIEC once again argues that only the initial nine pages of the formula rate tariff AIC filed be included and Appendices A and B to that filing be eliminated from the tariff. In the

Commercial Group's view, the point is well-taken and the Commercial Group supports IIEC's position.

e. Commission Conclusion

IIEC has proposed that the Commission exclude Appendices A and B from the tariff and adopt the nine tariff pages that AIC currently lists for Rate MAP-P itself. As the Commission understands it, both Staff and the Commercial Group supports IIEC's proposal regarding this issue on the level of detail.

AIC opposes the proposals to exclude portions of its proposed Rate MAP-P, arguing among other things that excluding details does not make the tariff less complicated and that consumers are free to ignore the details of the tariff if they so choose.

As an initial matter, the Commission notes that it addressed essentially the exact same issue only months ago in Docket No. 11-0721. While the Commission appreciates AIC's view on the issue, it has provided no meaningful reason that the Commission reach a different conclusion in this proceeding. As a result, because it is unnecessary to restate all of the positions in the record, or the full conclusion in Docket No. 11-0721, the Commission concludes that IIEC's proposal is the most reasonable and it is hereby adopted. Specifically, the Commission orders AIC to file Schedule FR-A1 and FR-A1 Rec. along with the Rate MAP-P tariff.

5. Proposed Rulemaking

IIEC recommends that the Commission initiate a rulemaking on the formula rate process, a recommendation which Staff supports. AIC, on the other hand, does not believe that such a rulemaking is necessary. In Docket No. 11-0721, the Commission adopted a similar IIEC proposal. In light of the need for such a rulemaking having been resolved in Docket No. 11-0721, the Commission finds that there is nothing to address in this docket on this issue of a formula rate process rulemaking. The rulemaking shall occur as called for in Docket No. 11-0721. AIC need not participate if it does not wish to, but it will be bound by any resulting rules.

6. Year-End versus Average Rate Base

a. AIC Position

AIC states that in providing for formula rates, the Act set forth an annual process by which formula rates are intended to be updated to reflect historical data from the most recently filed FERC Form 1, plus projected plant additions and correspondingly updated depreciation reserve and depreciation expense for the year of filing, and a reconciliation of the revenue requirement reflected in rates for each year, with what the revenue requirement would have been had the actual cost information for the year been available at the filing. It is AIC's position that the statutory language describing the reconciliation process plainly requires a year-end rate base for reconciliation.

AIC states that reconciliation is between a revenue requirement set using “cost inputs for the prior rate year” and an actual revenue requirement based on “the actual costs for the prior rate year.” According to AIC, the Act makes it clear that cost inputs are “final” data: “The inputs to the performance-based formula rate for the applicable year shall be based on final historical data reflected in the utility’s most recently filed annual FERC Form 1 . . . ” (AIC Initial Brief at 94, citing Section 16-108.5 (c)) AIC argues that an average rate base is not "final" data. AIC says the General Assembly specified that “the actual costs for the prior rate year” will be used. AIC says the actual costs for the prior rate year, as shown on FERC Form 1, are the final costs.

AIC contends that Section 16-108.5(c)(6) reinforces the “actual cost” concept by specifying an annual reconciliation “with what revenue requirement would have been had the actual cost information for the applicable calendar year been available at the filing date.” According to AIC, on or before May 1, 2013, a filing is made to set a 2013 rate year revenue requirement using 2012 actual costs plus 2013 plant additions. Had the actual cost information for 2013 been available at the May 1, 2013 filing date, AIC claims the actual information for the calendar year would reflect the year-end rate base. AIC claims that the General Assembly’s use of the words “final” and “actual” are in sharp contrast to Staff’s and Interveners’ “average” concept theory. AIC insists that “final historical data” and “actual costs” are simply not averages, as Staff and interveners suggest.

According to AIC, the statute provides that the reconciliation be calculated consistently with the initially established revenue requirement to which it is reconciled, and the initially established revenue requirement uses a year-end rate base. AIC says the statute also is clear that the reconciliation rely on FERC Form 1 data for the most recent calendar year before the year of the reconciliation filing and not an average calculated using the year before that and that year. In AIC's view, the Act requires a year-end rate base.

AIC contends this is confirmed by the fact that nowhere in Section 16-108.5 is the use of an average rate base specified. AIC notes the legislature has specified use of averages elsewhere in the Act and routinely used the concept of annual averages throughout the Act. AIC claims that as a matter of statutory construction, where the legislature includes particular language or terms in one section of a statute but omits it in another, it is generally presumed the legislature acts intentionally and purposely in the inclusion or exclusion of the different terms.

Citing Sections 16-108.5(c)(3)(A) and 16-108.5(b)(2) of the Act, AIC asserts that the General Assembly distinguished between where they intended an “average” to be used for a year and where they did not. AIC says Sections 16-108.5(c)(6) and 16-108.5(d)(1) do not contain the word “average,” and therefore the General Assembly did not intend the use of a reconciliation average rate base. AIC also says the legislature has often been very specific in how to calculate an average – yet no such specific calculations exist in the Act's reconciliation provisions. AIC believes that if the General Assembly intended to require the use of an "average" rate base for an applicable calendar year, it would have expressly used the term "average." In AIC's view, the absence of the use of the term average in the Acts' reconciliation provisions confirms that year-end rate base, not average, must be used for reconciliations.

The formula rate, AIC states, is designed to allow the utility to recover its actual costs incurred in a given year and reduce regulatory lag. AIC says those actual costs include the full amount of investment the utility made in the year. AIC believes appropriate ratemaking policy, and the need to ensure that customer rates are set to recover the costs of plant those customers are benefiting from, supports use of a year-end reconciliation rate base. AIC contends that use of an average rate base does not properly match the rates customers pay with the cost of plant from which they receive service.

AIC argues that the formula rate process is more like a historical test year, because it looks back to "actual cost information" for a prior, or historical year, the reconciliation year, at the time of reconciliation, is a fully historical period. AIC says the Commission has traditionally looked at year-end rate base for historical periods. Because the reconciliation period is a fully historical period, AIC believes use of a year-end rate base is appropriate to ensure a match between the rates paid by ratepayers and the cost of the plant used to provide them service at that time.

AIC argues that use of a year-end rate base ensures a match between the rates paid by ratepayers and the cost of the plant used to provide them service at that time. AIC develops an example of the annual update filed on or before May 1, 2013, with reconciliation being for the historical year 2012. At the conclusion of the annual update proceeding, AIC says new rates would go into effect for January 2014. AIC states that at the time the new rates go into effect reflecting the reconciliation, 2012 plant will have been fully in service for over a year. AIC believes rates should be set so that customers are paying for the full cost of this plant which is fully used and useful in serving them. AIC contends that use of an average reconciliation rate base, as Staff and interveners recommend, would create a situation in which ratepayers are not paying for the full amount of utility plant providing them service.

AIC contends that an additional policy benefit of using a year-end rate base is minimizing reconciliation balances. AIC alleges that if the initial or inception revenue requirement for a year is set using a year-end rate base, and is reconciled using an average rate base, there will always be a related impact on the reconciliation amount, equal to the revenue requirement associated with the difference between a year-end rate base and an average rate base (e.g., as much as half the projected annual increase in plant additions). AIC says this reconciliation amount will be larger than the reconciliation amount that would arise if AIC reconciles to a year-end rate base. AIC believes that in a year-end rate base reconciliation, the reconciliation amounts would reflect the smaller variance between the projected year-end rate base and the actual year-end rate base, which would be zero if projected plant additions and actuals are the same. AIC maintains that the use of a year-end rate base reconciliation will help minimize reconciliation balances and that use of an average rate base will increase reconciliation balances.

AIC also argues that use of an average rate base will result in AIC not recovering the difference between the average rate base amount and the year-end plant balance for the reconciliation period. AIC says the reconciliation will reconcile the projected year-end balance for the reconciliation year back to an average balance, resulting in an under-recovery for reconciliation rate base. In the subsequent rate year, AIC says rates will reflect the year-end plant balance of the reconciliation year plus projected plant additions for the subsequent year. By reconciling the reconciliation year rate base back to an average rate base, AIC claims the reconciliation revenue requirement will be understated once again. AIC says it will be forced to forego those dollars each year, as a permanent deferral, even though ratepayers were benefiting from a full year of the plant's service.

According to AIC, if the annual update filing is made on May 1, 2013, the rates will take effect in the rate year beginning January 2014 (and reflect actual 2012 costs plus projected plant additions for 2013). During the course of this 2014 rate year, AIC says it will also make additional plant investments, and that plant will be placed into service and will serve customers during 2014, although these 2014 additions will not be reflected in the 2014 rates. With respect to the reconciliation of the 2014 rate year (filed in 2015 and reflected in rates in 2016), AIC claims an average rate base methodology effectively halves the plant investments made during the course of the rate year, despite the fact that at the time the reconciliation rates take effect in January 2016, 100% of the investment was made and will have been providing service for over a year. AIC says this cycle will repeat itself each year resulting in a deferral of costs and ultimately an under-recovery by AIC. AIC contends that this exacerbates regulatory lag and denies full cost recovery, even though a purpose of the Act is to eliminate lag to the extent possible and to assure full recovery of reasonable and prudent costs.

AIC notes that a number of the parties rely on the Docket No. 11-0721 decision on the reconciliation rate base issue. AIC also notes that on June 22, 2012 the Commission granted ComEd rehearing on this issue. AIC suggests the underlying Order in Docket No. 11-0271 does not represent the Commission’s final word on the subject and thus cannot be used by the parties as an authoritative Commission pronouncement on the issue.

In response to IIEC's contention that formula ratemaking is still governed by Article IX of the Act as traditional ratemaking was, AIC claims the Public Acts 97-0616 and 97-0646 represent a fundamental change in the regulatory structure governing how rates are set for participating utilities. AIC argues that because the Commission has only the power granted it by the legislature, the Commission must follow the requirements of the Act. AIC contends that Public Acts 97-0616 and 97-0646 represent a more recent, specific legislative scheme applicable only to certain participating electric utilities for setting utility rates. AIC says Article IX represents the more general rate setting scheme applicable to other utilities which are not participating utilities. According to AIC, the Act establishes a specific process whereby participating utilities' actual costs for each year are to be recovered through a reconciliation process, and sets out specific protocols for the setting of ROE and the recovery of certain types of costs. AIC argues that Public Acts 97-0616 and 97-0646, as the more recent and specific set of statutory provisions, controls over Article IX. AIC insists that contrary to IIEC's assertions, the provisions of general applicability, Section 9-211, does not control the specific requirements regarding setting and reconciling the formula rate base set forth in Public Acts 97-0616 and 97-0646.

AIC concedes that although Public Acts 97-0616 and 97-0646 do reference Article IX, its application is more limited than IIEC argues. AIC says Article IX is referenced three times in material relation to the setting of formula rates. First, when the Commission reviews the utility's initial tariff setting out the formula rate structure and protocols, "the Commission shall initiate and conduct an investigation of the tariff in a manner consistent with the provisions of this subsection (c) and the provisions of Article IX of this Act to the extent they do not conflict with this subsection (c)." AIC contends that IIEC's read of Section 9-211 does create a conflict, because IIEC reads Section 9-211 as requiring use of an average rate base. In AIC's view, the language of Section 9-211 supports use of a year-end rate base, because, at the time rates are in effect, over a year after the year being reconciled (e.g., the rates resulting from the reconciliation of 2013 will be established in 2014 and go into effect January 1, 2015), the "value of such investment which is both prudently incurred and used and useful in providing service" will be the year-end value. AIC insists that under the Act itself and the principles of statutory construction, Section 9-211 must yield to the requirements of Public Acts 97-0616 and 97-0646.

AIC indicates that IIEC notes in its Initial Brief the Act requires the review of initial formula rates and subsequent updated cost inputs to be "based on the same evidentiary standards, including, but not limited to, those concerning the prudence and reasonableness of the costs incurred by the utility, the Commission applies in a hearing to review a filing for a general increase in rates under Article IX of this Act." AIC claims that IIEC does not cite "evidentiary standards" in support of its position, it cites the legal standard of Section 9-211.

AIC suggests that the position of parties, including IIEC, AG/AARP, and the Commercial Group, are based in part on a misunderstanding of the difference between a "rate year" under Public Acts 97-0616 and 97-0646 (the year rates are in effect) and the year for which projected plant additions are estimated and ultimately reconciled (the year in which a formula rate initial or update filing is made). AIC states that the rate year is the year rates are in effect, so for example, AIC would file updated cost inputs in May 2013, plus projected plant additions through 2013, and a reconciliation of 2012 costs.

According to AIC, AG/AARP appear to have a similar misunderstanding, stating that, "In May of 2013, the Company will again reset inception rates that will be charged beginning in January 2014, based on FERC Form 1 2012 actual cost inputs, projections of net plant additions expected in 2014 and with a reconciliation of the Company's 2012 actual revenue requirement to the revenue requirement(s) that were effective during 2012 on a weighted basis." (AG/AARP Initial Brief at 8) AIC argues that under the Act, the projected plant additions would be for the year in which the inputs are filed, or in the AG's case, 2013, not 2014.

AIC alleges that correcting AG/AARP's and IIEC's understanding of the formula rates process supports its position on use of year-end rate base. AIC says rates in effect in the rate year (2014) will be recovering costs as established in a 2013 filing, using data from the most recently filed FERC Form 1 (2012) and projected plant additions and correspondingly updated depreciation reserve and expense for the calendar year in which the inputs are filed, or 2013. AIC adds that when rates go into effect in 2014, the 2013 plant additions have been completed, been paid for, and will be used and useful in providing service, so use of a year-end rate base is appropriate to match customers rates with the plant providing them service. AIC says in the May 1, 2014 update filing, costs and rate base for the prior rate year (2013) will be reconciled, with rates going into effect in the rate year 2015. AIC claims that at that time, over a year will have elapsed since the plant investment was made in 2013, so the reconciled customer rates will still be recovering costs for plant additions completed and in service.

AIC states that the Commercial Group, although correctly noting that the cost information is for the "applicable calendar year," misinterprets AIC's position as suggesting that the revenue requirement is being established for the year rates are in effect (2014). AIC says the revenue requirement is being estimated for the applicable calendar year (2013), and it is that year whose revenue requirement will be reconciled in the 2014 update filing under Section 16-108.5(d)(1) of the Act. According to AIC, the rate year would be the year following the year updated cost inputs are filed. AIC claims there is nothing unusual about a revenue requirement being set based on one year with rates effective in a different year, a traditional historical test year will be for a year that ends before the year rates go into effect to recover the revenue requirement set based on that year. AIC says it filed a rate case in 2009 using a 2008 test year, for which rates went into effect in 2010.

AG/AARP also allege that use of a year-end rate base results in customers paying a return on investment before it is made. AIC insists the opposite is true; customers will not be paying for an investment until after it has been made and is used and useful in providing service. AIC contends that Staff and interveners' argument continue to discount the important policy consideration that the customer rates should reflect the cost of plant being used to provide those customers service.

AIC says AG/AARP argue that discussions of traditional test year ratemaking are not applicable in the context of formula rates while, IIEC argues that the Commission's review of the average versus year-end rate base issue should involve issues or approaches common to Article IX reviews of test year rate case proposals, suggesting comparisons to traditional ratemaking models is appropriate. According to AIC, it is instructive to compare the ratemaking theory behind traditional models with formula rates. AIC maintains the formula rate process is more like a historical test year, because it looks back to “actual cost information” for a prior, or historical year, the reconciliation year, at the time of reconciliation, is a fully historical period. AIC says that like historical test years, a “pro-forma” adjustment is made for projected plant additions through the year in which a rate update filing is made. AIC maintains that the Commission has traditionally looked at year-end rate base for historical periods. Because the reconciliation period is a fully historical period, AIC believes use of a year-end rate base is appropriate to ensure a match between the rates paid by ratepayers and the cost of the plant used to provide them service at that time.

According to AIC, CUB, AG/AARP and IIEC argue that use of a year-end rate base will cause AIC to over earn its revenue requirement. AIC contends it will in fact be adversely impacted by the use of an average reconciliation rate base. AIC says AG/AARP, in particular, seem to believe that AIC will have unlimited upside to over earn its rate of return, with “even larger” variances than AG/AARP discuss. AIC claims this ignores the Act’s ROE “collar,” which limits AIC’s earned return on common equity to 50 basis points above or below the return on common equity set by formula. With this provision, AIC asserts that the Act mitigates any concern that AIC will over-earn its revenue requirement in the manner AG/AARP suggest.

b. Staff Position

According to Staff, while the Act does not specifically state that either year-end or average rate base should be used in determining the reconciliation revenue requirement, the Act is specific and consistent in requiring actual cost information be used for the applicable calendar year, and not “as of” the applicable year-end. Staff claims the specific language of the Act bears the interpretation that the reconciliation revenue requirement is to be calculated for a period of time, not as of a particular point in time.

Staff asserts that the record is clear that average rate base can be calculated from cost information “reflected” in FERC Form 1. Staff says the FERC Form 1 for any given year includes both the plant in service balance at the beginning of the year (page 204 and page 206) and at the end of the year (page 205 and 207); thus, a revenue requirement using average rate base can be calculated using information “reflected” in FERC Form 1. Staff also claims that operating and maintenance costs “reflected” in FERC Form 1 are “for” the calendar year, so those costs more closely match the average plant in service for the calendar year.

Staff says that when addressing the same issue in Docket No. 11-0721, the Commission adopted the proposal made by AG/AARP and others to compute the reconciliation rate base using an average. Staff acknowledges that this is still at issue in the rehearing phase of the ComEd proceeding. Until such a time as the Commission issues an order on rehearing determining that an average rate base should not be used, Staff says the May 29, 2012 Order remains in effect and should be consistently applied in this similar proceeding. Staff claims it would be unreasonable for the AIC formula rate, which is based upon the same statute as ComEd's, to contain a different conclusion on the same issue as ruled upon in Docket No. 11-0721.

c. IIEC Position

IIEC states that by its terms, the formula rate statute is intended to assure timely recovery of a participating utility's actual costs. IIEC suggests that AIC's construction of the statute bases formula rates on data remote from and unrelated to the actual costs in the rate year, purportedly underlying the rates. IIEC asserts that whether the elements of AIC's proposed implementation of the Act are considered in isolation or comprehensively, AIC's proposed implementation is not sensible.

IIEC argues that the Commission's construction of the formula rate statute in the ComEd formula rate case arose from the language of the statute itself and implicitly rejects AIC's statutory construction. IIEC notes that the same formula rate statute applies to both AIC and ComEd, and suggests that disparate constructions of the same language for the two participating utilities would be unlawful and unsupported, as AIC has identified no differences between the utilities that would support distinct implementations of formula rates for ComEd and AIC. Despite allusions to such differences, IIEC states that the only difference AIC has identified is its status as a combination utility which is associated with distinct investment (but not formula rate) provisions.

IIEC notes that AIC proposes to use the reported end-of-year investment in its FERC Form 1 as the principal basis for calculating its rate base for setting initial formula rates and for reconciliation of revenue requirements for the rate year. IIEC witness Gorman, however, opposes AIC's proposed use of the likely highest investment amount in a rate period, as the rate base for the entire period and the foundation of formula rates for that period. IIEC argues that using the reported year-end amount as AIC proposes would overstate the investment AIC actually has in service during the rate period. IIEC instead proposes the consistent use of an average year rate base, for both initial rates and reconciliation. IIEC proposes specifically that the Commission use an average year rate base, calculated using the January 1 and December 31 investment amounts shown on the relevant AIC FERC Form 1. IIEC notes that other parties recognize that AIC's actual capital costs are not determined by the size of its changing rate base on December 31 of each year, but propose its use only for the reconciliation process.

In response to other parties' objections, IIEC opines that several AIC witnesses make a series of arguments in defense of AIC's decision to use its year-end investment amount as the base amount for determining its rate setting and reconciliation costs. IIEC notes that AIC contends that: (i) the year-end amount is required by Section 16-108.5(c)(6); (ii) an average year rate base is not explicitly mentioned in Section

16-108.5; (iii) the initial rate and cost determinations must use the same calculation method; and (iv) rates set using an average year rate base do not match AIC's costs while those rates are in effect. IIEC argues that each of those arguments is without substantive or legal merit.

IIEC notes that there appears to be a firm consensus among the parties that the Commission should seek to approximate, as closely as practicable, AIC's actual costs for the rate period at issue. IIEC states the issue on which application of that principle is most consequential is in the determination of AIC's rate base. IIEC asserts the disputed issues are whether a year-end or average year calculation accomplishes that goal and whether success should be measured against costs during the year for which costs are determined or the year in which rates are effective.

IIEC claims that AIC's legal arguments lack a basis in Section 16-108.5, which defines, as the over-arching objective of formula rates, that "the formula rate approved by the Commission shall . . . (1) provide for the recovery of the utility's actual costs of delivery services that are prudently incurred and reasonable in amount consistent with Commission practice and law." (Section 16-108.5(c)) IIEC notes that Section 16-108.5(d), which states that the intent of the reconciliation is to reconcile the revenue requirement reflected in rates for each calendar year with actual cost information for the applicable calendar year, and IIEC states AIC does not dispute this "actual cost" focus of the statute. And though AIC's FERC Form 1 is identified as the starting point for formula rate cost inputs, IIEC claims that Section 16-108.5(c) is equally clear that the mere presence of a number in that form has no determinative significance.

IIEC opines that Section 16-108.5(c) requires that a participating utility determine its initial formula rates using "final data based on its most recently filed FERC Form 1," plus cost projections for the following rate year. Similarly, IIEC notes the formula rate cost inputs in subsequent reconciliation proceedings must be "based on final historical data reflected in the utility's most recently filed annual FERC Form 1," plus projected costs for the following rate period.

IIEC asserts that in both initial and reconciliation formula rate proceedings, all proposed cost inputs, whether or not shown on a FERC Form 1, are expressly subject to the Commission's Article IX authority and duty to ensure that only prudently incurred, reasonable costs are included in approved rates. IIEC claims that such review shall be based on the same evidentiary standards, including, but not limited to, those concerning the prudence and reasonableness of the costs incurred by the utility, the Commission applies in a hearing to review a filing for a general increase in rates under Article IX of this Act.

IIEC states that the Commission shall apply the same evidentiary standards, including, but not limited to, those concerning the prudence and reasonableness of the costs incurred by the utility, in the hearing as it would apply in a hearing to review a filing for a general increase in rates under Article IX of this Act. In response to criticisms from other parties regarding its proposed use of year-end rate base amounts, IIEC notes that AIC turned to test year analogies to support its position.

IIEC opines that AIC agrees that the formula rate regime is not a test year process, which sets rates for an indefinite period, but a process that has at its core the determination and recovery of AIC's actual cost of service for a single, specific year. IIEC's Mr. Gorman explained that in contrast, a formula rate, including the reconciliation charge or credit, is designed to recover the utility's actual and prudent cost within a specific rate year. Mr. Gorman notes that while the rates may be in effect for some period beyond the rate year does not change the fact that the formula rate is designed to recover the cost within the rate year, and is not being used as a proxy to estimate future cost of service during the period rates are in effect.

Under the governing statutory process, IIEC states that AIC will recover its actual prudent and reasonable costs for each year, regardless of when collections begin, because projected investment data is used to develop an initial revenue requirement and rate, which are fully reconciled, after the fact, to a revenue requirement based on the actual cost data. And that reconciliation includes compensation for the delay in cost recovery. IIEC opines that when AIC tests the proposals for average or year-end rate base amounts, it does not ask whether the formula rate recovers that specific year's cost in full, but not excess. Instead, IIEC suggests that AIC asks whether the rates to recover that specific year's costs match the utility's costs for the later year when the rates are in effect, which IIEC argues is the wrong question.

Contrary to the argument AIC makes in defense of its proposal to use year-end rate base amounts, IIEC avers that it is apparent that neither average year nor year-end rate base amounts are expressly mentioned or required by Section 16-108.5. While AIC witness Nelson argues that nowhere in Section 16-108.5 does it specify the use of an average rate base; IIEC asserts that it is equally true that the statute makes no mention of "year-end" rate base in its directives for the determination of revenue requirement, for either initial or reconciliation formula rates.

Since the formula rate statute does not expressly require the use of either average-year or year-end amounts, IIEC claims that the Commission's determination of AIC's actual, prudently incurred, and reasonable investment in its Article IX review is the decisive factor. IIEC states that the Commission's deliberations should involve issues or approaches common to its Article IX reviews of test year rate case proposals, and the Article IX determinations must be based on the substantive record evidence in this case. IIEC suggests that the evidence presented supports IIEC's recommended modifications of AIC's proposed rate base computation.

IIEC witness Gorman argues that an analogy of the "average" versus "year-end" rate base amounts would be where and an investor deposits $100 per month in a bank account paying interest at 12% per annum. IIEC states the incremental deposits are analogous to AIC's plant investments, and the interest rate to Ameren's return or cost of capital. IIEC asserts that AIC's year-end proposal would have the interest earned calculated as though the depositor deposited all $1200 on January 1, while an average year calculation would recognize the gradual accretion of funds by calculating the interest earned using the average amount on deposit during the year.

Regarding the rate base to be used in setting AIC's formula rates, IIEC avers that the record in this case establishes that an average rate base is the more accurate measure of AIC's changing investment over the course of a year, and thus its actual costs with the rate year. IIEC claims that the dynamic nature of AIC's investment amount is confirmed by its own testimony and validates the average year rate base as the amount properly used in setting AIC's formula rates.

IIEC states that the value of plant investment AIC actually uses to provide service during the year may not reach the December 31 level until the end of the year. IIEC opines that setting rates using AIC's larger year-end rate base for the entire year overstates the rate base, AIC's costs and thus AIC's rates, in violation of Article IX requirements respecting rate base actual costs and rates.

To justify its proposal to use a year-end figure, thus yielding a larger rate base, IIEC notes that AIC turns to test year concepts it rejected when it chose the distinct, fundamentally different formula rate process. IIEC suggests that while AIC argues instead for a calculation of its capital costs based on "the full expenditure of cost related to plant as of 12-31," Mr. Nelson's own testimony confirms that AIC increases plant only gradually throughout the year. IIEC contends that setting rates based on a year-end rate base exaggerates the investment AIC actually used to provide service for 364 days of the year, overstates its actual rate year costs and produces unlawfully inflated rates.

d. The Commercial Group Position

The Commercial Group states that it is well-settled that the Commission can and should use its rate-making expertise in implementing statutory utility rate provisions that are not crystal clear on their face, citing Illinois Consolidated Telephone Co. v. ICC, 95 Ill. 2d 142, 152 (1983). With respect to the formula rate statute, the Commercial Group argues the General Assembly defined certain terms with particularity but left other terms more general. In setting the initial revenue requirement and in determining the reconciliation charge, the Commercial Group notes the statute nowhere uses the terms "end-of-year rate base" or "average rate base" even though those terms are standard rate-setting terms; therefore, the Commission must use its rate-making expertise to fill in such blanks in the statute.

The Commercial Group believes the clearest statutory provision is the best starting place for interpretation, and in doing so, the Commission should start by correctly interpreting and implementing the clearest of the relevant revenue requirement provisions – the reconciliation revenue requirement – and working backward from there to the less-clear provisions. Fortunately, the Commercial Group believes the legislature made doubly clear in Section 16-108.5(d)(3) - by the phrase "Notwithstanding anything that may be to the contrary" - that the overriding purpose of the reconciliation is to compare the revenue requirement reflected in rates for each calendar year “with what the revenue requirement would have been had the actual cost information for the applicable calendar year been available at the filing date.” The Commercial Group suggests that the purpose for reconciliation then is not, as AIC would have the Commission believe, to reflect what the revenue requirement should be in the year when the rates are in effect, which (in terms of the statute) is the year after “the applicable calendar year.” The Commercial Group notes the General Assembly could have stated, but did not state, what AIC alleges. The Commercial Group acknowledges that the Commission is bound to follow the words of the statute and not some later statement by the utility that the words of the statute are other than they are.

The Commercial Group believes the relevant question is what the revenue requirement would have been in that calendar year if the actual cost information been known. With respect to rate base, the Commercial Group suggests knowing the rate base totals at a daily, weekly or monthly basis during the calendar year would best capture the return the utility would have earned on that rate base over the course of the year, and hence, what the revenue requirement would have been. The Commercial Group notes the statute also states that FERC Form 1 data be used. Given that this FERC form has beginning and end of year figures on it (and not daily, weekly or monthly figures), the Commercial Group asserts the only options are to use the beginning of year balance, the end of year balance, or both of these figures. The Commercial Group opines that AIC witness Nelson admitted that in an escalating investment period such as contemplated by the formula rate statute, an end-of-year rate base would include projects not in service earlier that year. Thus, the Commercial Group claims that an end-of-year rate base would overstate rate base during the calendar year, while on the other hand, a beginning-of-year rate base would understate the rate base during the calendar year. The Commercial Group argues that averaging the beginning and end-of-year balances would more closely approximate the rate base over the entire calendar year, therefore the reconciliation revenue requirement must be based on an average of the rate base data in FERC Form 1.

Having started from the clearest of the revenue requirement provisions, the Commercial Group indicates that a remaining question with respect to rate base is whether the projected plant additions for setting the initial rates should be averaged over the calendar year, as proposed by IIEC, or totaled for the entire year as proposed by a number of other parties. The Commercial Group believes that using an average projected year to set the initial rate for the calendar year makes the most logical sense since it mirrors the average-year reconciliation rate base that is required by the statute. The Commercial Group believes this would eliminate what AIC alleges is a mismatch of calendar year data, therefore, the Commercial Group supports the IIEC position on this issue.

The Commercial Group also recognizes that there is no "notwithstanding anything that may be to the contrary" language in the non-reconciliation portion of the statute and the Commission accordingly has more discretion to decide how to set the initial rates. Notably, unlike the after-the-fact actual costs used for reconciliation, the

Commercial Group notes that projections are by their nature uncertain. Given the inherent uncertainty of projections and given that a later reconciliation will occur, the Commercial Group suggests it may not be unreasonable to include all of the reasonable and prudent projected capital expense in the calendar year into rates for that year, as the Commission decided to do in the ComEd Rate Order (i.e., the Commission's final order of May 29, 2012 in Docket No. 11-0721). The Commercial Group opines that this methodology also addresses the utility's concerns for an earlier start for receiving a return of its investment in new plant.

The Commercial Group notes that AIC has complained about the Commission's decision in Docket No. 11-0721 adopting an average year rate base for reconciliation. The Commercial Group avers that AIC believes the Commission, by the Order in Docket No. 11-0721, is trying to impose on ComEd and AIC a cost recovery method that is significantly less favorable than under pre-existing law, and would withhold from the ComEd and AIC the financial tools and resources needed to undertake the obligations under the law successfully and allow them to maintain their financial integrity. The Commercial Group opines that this position of AIC is not supported by the record, and instead, the formula rate statute, as interpreted by the Commission in Docket No. 11-0721, provides the utilities many advantages over the traditional rate regulation that AIC decided to avoid.

The Commercial Group notes that AIC recovers its incremental capital investment cost sooner and with more certainty under the new formula rate regulation as interpreted in the ComEd Order than under traditional rate regulation. Nevertheless, the Commercial Group states that when AIC was on the verge of capturing its investments in rate base through traditional rate regulation, AIC abandoned that process in mid-stream by dismissing Docket No. 11-0729 and opting for the new regulatory scheme, although AIC now complains about the new formula rate process whereby AIC's rates for "the calendar year" include an amount in rate base that exceeds its actual investment level throughout that calendar year. The Commercial Group argues that AIC determined that the pre-existing law of traditional rate regulation was more or less favorable to AIC than the new rate formula law, noting that AIC opted to withdraw its rate application in Docket No. 11-0279.

As the Commercial Group has stated, the Commission could reasonably match an average projected rate base for the initial rates for the calendar year with an average-year reconciliation rate base. In that instance, if AIC's projections match its actual investment, the Commercial Group recognizes that there would be no reconciliation for a rate case difference. The Commercial Group believes that the methodology of the ComEd Rate Order is more favorable to AIC in that the initial rate base would be inflated to include all of the projected capital investment and allow AIC to earn a return on all of that investment throughout the calendar year rates are charged. Further, when the reconciliations take effect to return the rate base to what the rate base would have been if all the actual cost information had been known, the Commercial Group avers that rates would bump up again to include all of the projected capital additions for the subsequent calendar year. The Commercial Group asserts that

AIC would be given all of the benefit of the doubt in projections for that next calendar year and throughout the next year earns a return on all of its projected investment made during the calendar year, even though its rate base levels during that year would have been lower.

The Commercial Group notes that the Order in Docket No. 11-0721 would allow an interest rate on the rate base reconciliation amount that is less than AIC's weighted cost of capital. The Commercial Group suggests that with respect to rate base, this interpretation by the Commission favors the utility in that the utility would have earned a return of approximately nine percent (weighted cost of capital) on 100% of its projected capital investment throughout the year rates are in effect and then only have to return to ratepayers interest at the lower weighted cost of debt.

The Commercial Group states that the new model eliminates a significant area of dispute in traditional rate cases, the dispute over ROE. In this formula rate case, both Staff and AIC agree on a ROE of 10.05%. The Commercial Group avers that partly because of the change in how ROE is determined, there also is a much narrower disagreement over the initial revenue requirement to be established in this formula rate proceeding than in prior rate cases. The Commercial Group also claims that another benefit to AIC is that AIC's ROE can be adjusted after-the-fact if it earns 50 basis points less than its authorized return. This contrasts sharply with Mr. Nelson's testimony in Docket No. 11-0279 that none of the AIC companies had earned their authorized ROE during parts of 2009 and 2010.

The Commercial Group opines that all of these benefits to the utility mean that Mr. Nelson's claim that this new formula rate system is less favorable than the traditional rate regulation that AIC eschewed, is apparently designed to intimidate the Commission to back-track from its reasonable decision in the ComEd Order. The Commercial Group contends that the new system already favors the utility, and suggests that AIC simply wants the scale to be tilted even more in its favor by setting formula rates to earn a return on a rate base that is inflated over actual cost during the statute's "calendar year." The Commercial Group recommends that the Commission's decision comport with the statute and set rates based on an average year rate base.

e. AG/AARP Position

According to AG/AARP, AIC's ability to recalculate its annual revenue requirement retroactively and recover the difference between the inception revenue requirement (based on the prior year FERC Form 1 data plus projected plant additions) and that same year's FERC Form 1-derived actual revenue requirement is a major change in regulation. AG/AARP believe this true-up process changes a fundamental effect of the prior regulatory system because it allows AIC to retroactively charge or credit consumers for changes in its costs that occur after the rate is set, effectively eliminating all regulatory lag while shifting responsibility for changing costs entirely onto ratepayers. AG/AARP also believe test year principles must be rethought in order to accommodate this change in the law and the framework of Illinois regulation.

AG/AARP state that traditionally, a utility's revenue requirement is set pursuant to test year rules to estimate the utility's annual revenue needs for an indefinite future. By law, AG/AARP say the revenue requirement cannot be changed retroactively. By contrast, AG/AARP indicate that the inception revenue requirement set under Section 16-108.5 is designed to be serve as an interim revenue requirement, subject to modification after actual cost data is available on the FERC Form 1, with interest added to any over or under-recoveries of actual costs.

According to AG/AARP, each May 1st, AIC proposed to file its calculation of prospective changes to the formula rate revenue requirement using inputs from the prior year's FERC Form 1 and other data sources. If the actual FERC Form 1 data for the revenue requirement year produces a higher revenue requirement than the previously established inception revenue requirement, AG/AARP say the difference (with interest) is added to the rates consumers pay in the next annual set of rates. AG/AARP indicate it is also possible for the actual revenue requirement to be lower than the inception rates, although AG/AARP expect revenue requirement increases, not decreases, due to the incremental, large investment commitments contained in the Act.

AG/AARP believe the question of whether the rate base to which the utility's cost of capital is applied should be measured as an average or at year-end must be carefully considered in light of this new regulatory structure. AG/AARP say the Commission has historically allowed year-end rate base when setting prospective revenue requirements so as to reduce the regulatory lag inherent in traditional regulation. AG/AARP assert that under the Act that now allows the full recovery of costs that deviate from the inception revenue requirement, with interest, the traditional "regulatory lag" resulting from the use of a historical test year and the need to wait eleven months to change tariffed rates is eliminated.

AG/AARP state that in determining the inception revenue requirement (e.g. for 2011), the formula rate utilizes an end-of-year rate base taken from the prior FERC Form 1 year (2010), plus plant additions (for 2011). AG/AARP contend that the inception revenue requirement does not represent the final amount of revenues that consumers will provide the utility for the year. While using the end-of-year rate base and including the coming year's plant additions minimizes the expected difference between the reconciliation revenue requirement and the inception revenue requirement, AG/AARP say the reconciliation revenue requirement is the final calculation that must necessarily account for actual incurred levels of cost, including actual expenses throughout the year and actual net investment requiring a return throughout the year. AG/AARP state that the use of an end-of-year rate base (from the former year) in determining the inception revenue requirement is the first step in estimating that year's revenue requirement that will be later subject to reconciliation, but they claim it does not compel the use of an end-of-year rate base in the calculation of the reconciliation. AG/AARP contend the reconciliation revenue requirement and the inception revenue requirement have different functions, use different data sets, and produce different results.

AG/AARP argue that using an average rate base in the reconciliation year will properly quantify capital costs as they accumulate over the year rather than as a point in time (end-of-year), better matching the other elements of the revenue requirement and income in a given year. AG/AARP contend the proper level of return for investors should reasonably compensate the actual level of capital invested in the delivery service business throughout the true-up period. If the rate base were calculated as of year-end, AG/AARP claim consumers would pay a return on the total annual as if that amount were funded (and a return needed) every day of the year. AG/AARP claim the investment can be expected to be made ratably over the course of the year – not on January 1. AG/AARP say the average rate base measures the net investment in facilities to provide utility service over the course of the year, rather than as of a point in time as of the end of the year. AG/AARP assert that AIC's investment in assets serving delivery service customers is generally higher at year-end than throughout the reconciliation year. AG/AARP add that the effect of using a year-end rate base is to improperly treat investment as of December 31 as if it had been made the prior January 1. AG/AARP believe this results in consumers paying a return on investment before it is made and will systematically overstate the capital cost charged to consumers.

AG/AARP contend the average or year-end rate base approach to the calculation of the reconciliation revenue requirement is an important issue in the establishment of the formula rate process because AIC is committing to making incremental investments in electric system upgrades estimated at $625 million over ten years, with $265 million for the purpose of electric system upgrades and $360 million for smart grid deployment. According to AG/AARP, these "incremental" investments totaling $625 million are above and beyond AIC's normal pace of spending to accommodate replacement of aging plant, customer growth and other ongoing capital programs. AG/AARP aver that if one assumes ratable capital spending and the impact of only the incremental investment commitments in years one through ten of the program, annual rate base growth caused by the new investments could average about $62 million per year. AG/AARP claim the "value" of reconciling the revenue requirement using year-end versus average rate base would be approximately one-half the ratable investment growth expected each year, since the mid-point of spending in a typical future year could be at the $31 million level of plant additions, while by year-end plant additions could total the $62 million. AG/AARP contend that translating this typical rate base difference of $31 million into revenue requirement would produce additional annual revenues for AIC after reconciliation of approximately $4.4 million per year.

With persistently growing future rate base investment levels, AG/AARP contend there is no doubt that using a year-end rate base in the reconciliation of annual revenue requirements will overstate charges to customers and inflate AIC's return on actual investment, relative to the actual cost of capital for the year being examined. AG/AARP provide an illustration which they claim shows the post-tax return available for ROE capital exceeds the intended ROE by approximately 41 basis points each year, adding about $5 million of return costs, plus the related factor-up for income taxes, to the revenue requirement burden faced by ratepayers. AG/AARP argue that if rate base grows more rapidly than five percent per year, the ROE variance relative to intended earnings levels would be even larger, and vice-versa. Given the specific statutory formula for determining AIC's cost of equity, AG/AARP believe the Commission should not allow an inadvertent increase in the authorized profit level by using year-end rather than the more representative average rate base for determining the actual, reconciled revenue requirement.

AG/AARP assert that the utility's actual investment in new plant and the corresponding growth in newly invested equity and debt capital tend to grow gradually throughout the year. They say the associated return requirement for such capital also grows gradually throughout the year. If the revenue requirement calculation is based upon the year-end level of such rate base investment, as if that investment were fully incurred on January 1 and existed in all months of the test year, AG/AARP argue the resulting return requirement is systematically overstated. They say this is the financial result caused by AIC's proposal to utilize a year-end rate base within the reconciliation process.

AG/AARP contend the only valid reason for employing a year-end rate base in an otherwise average test year approach is to reduce regulatory lag by approximately six months, which is the difference between the mid-point of an historical test year and year-end. AG/AARP say that when a year-end or "annualized" rate base is used by regulators, it is common for other elements of the revenue requirement such as wage rates, employee headcounts, customer counts, depreciation expense and other known changes to be similarly annualized at year-end. They claim the combined impact of such broadly applied annualization adjustments is to reduce regulatory lag.

If AIC's revenue requirements are to now be annually trued-up, so as to fully recover jurisdictional actual incurred costs, AG/AARP insist there is no need to address regulatory lag through use of a year-end rate base. They say traditional test-year regulation involves setting utility rates that remain unchanged until the "next" rate case is filed, causing regulatory lag to exist when cost changes occur between test year rate cases. AG/AARP contend regulatory lag concerns are completely mitigated by the new formula ratemaking regime, where AIC will be made "whole" with interest for changes in all of its actual jurisdictional costs incurred to provide delivery services in Illinois. When the formula-based revenue requirements, which are inclusive of projected net plant in service additions, are trued-up through the reconciliation process to actual cost levels, AG/AARP claim any revenue requirement variances are allowed interest charges to be sure that regulatory lag imposes no financial consequences on AIC. In this new regulatory environment, AG/AARP believe there is no need for the Commission to permit the use of year-end rate base as a remedy for regulatory lag.

AG/AARP state that AIC argues that a year-end approach should be used. AIC asserts that an average reconciliation rate base concept is not provided for, or consistent with, the provisions of Section 16-108.5 of the Act. AG/AARP say AIC complains that the use of an average rate base is inconsistent with the Commission's treatment of historical annual periods in traditional ratemaking, and argues that an average approach creates a mismatch between rates that customers pay and the cost of plant to provide them service and produces an under-recovery for reconciliation rate base. AG/AARP say that a search of Section 16-108.5 of the Act reveals no reference to use of either an average or an end-of-year rate base approach to reconciliation. AG/AARP conclude that it is within the Commission's authority and discretion to resolve the issue. AG/AARP also say the Commission addressed the issue of whether an average reconciliation rate base is consistent with the Act in Docket No. 11-0721.

AG/AARP indicate that AIC witness Nelson quotes from Section 16-108.5(d)(1) which states, "The inputs to the performance-based formula rate for the applicable year shall be based on final historical data reflected in the utility's most recently filed annual FERC Form 1 . . . ." According to AG/AAR, this language does not preclude use of average rate base calculations in the reconciliation process. AG/AARP claim all of the information required to calculate an average rate base can be derived from final annual FERC Form 1 data. AG/AARP say for most elements of rate base the data presented within the FERC Form 1 contains both beginning of year and end of year balances to support such an average calculation.

AIC asserts that an average rate base is only appropriate with a future test year because, with a future test year, new rates will typically go into effect early in the future test period – in other words before the full investment cost for the test period has been incurred and before all plant projected for in the future period is in service. AIC believes an average rate base is reasonable because again it matches the rates paid by utility ratepayers with the cost of the plant actually providing them service.

AG/AARP state that the revenue requirement reconciliation process required under the Act ensures a complete matching of rate and revenue levels with the cost of actually providing service during that same period and provides for the accrual of interest on any difference between actual costs and allowed revenues. AG/AARP believe that in this context, AIC's discussion of future versus historical test years is not applicable because the reconciliation process is designed to ensure a full matching of revenues with overall actual costs without regard to how rate and revenue levels were initially set. AG/AARP assert the key question is whether average or year-end investment levels are most indicative of the utility's actual deployed investment throughout the reconciliation year. Given AIC's gradual investment pattern throughout a given year, AG/AARP believe an average rate base is appropriate.

AIC complains that the use of an average reconciliation rate base would create a mismatched result, by reconciling an estimated revenue requirement initially calculated assuming a year-end rate base, to a subsequent calculation using a fully historical period and an average rate base. AG/AARP claim this is a straw man argument. They assert that no mismatching is created by preparing the estimated revenue requirement initially calculated using a year-end rate base approach and then reconciling such estimates using an average rate base approach. According to AG/AARP, the reconciliation procedure will make AIC whole for its actual costs incurred to provide service, plus interest that is to be accrued on any amounts over or under-recovered.

AG/AARP believe that any mechanical differences that may exist in the determination of the inception versus the reconciliation revenue requirement are significant only to the utility's cash flow and do not affect to its earnings due to the fact that the statute provides for interest during the period that reconciled revenue requirement amounts have not yet been credited or charged to customers.

AG/AARP say that AIC complains reconciling to an average rate base, will likely result in AIC simply not recovering the difference between the average rate base amount and the year-end plant balance for the reconciliation period. AG/AARP assert that AIC should not be allowed to recover a return on more invested capital than actually exists throughout the period being reconciled. AG/AARP claim this is the point of using an average rate base -- to better quantify AIC's actual invested capital throughout the reconciliation year. They claim AIC should be required to forego those dollars each year that result from utilization of a year-end rate base because AIC's year-end investment levels are not representative of actual invested capital earlier and throughout the same year.

AG/AARP state that AIC has proposed a spreadsheet template to document the calculation steps to be employed in administering Rate MAP-P. AG/AARP believe that a few simple revisions to this template are needed to ensure that the reconciliation of revenue requirements is performed using an average rate base approach. AG/AAARP say the same template changes were ordered by the Commission for implementation by ComEd in Docket No. 11-0721.

AG/AARP assert that contrary to AIC's arguments, the plain language of Section 16-108.5 of the Act supports use of an average rate base in annual reconciliations – not use of a year-end rate base. AIC asserts that the Act makes it clear that cost inputs for reconciliations are "final" data, relying on the phrase "final historical data" as support for its position. According to AG/AARP, the reference to "final historical data" in Section 16-108.5(d)(1) actually refers to the filing of the formula rate for the applicable year – not the reconciliations. AG/AARP agree that initial formula rates should incorporate end-of-year rate base figures. AG/AARP argue the General Assembly was clear in plainly stating that the reconciliation of the revenue requirement that was in effect for the prior year shall be based on the "actual revenue requirement for the prior rate year." They say the Act provides that "the intent of the reconciliation is to ultimately reconcile the revenue requirement reflected in rates for each calendar year, beginning with the calendar year in which the utility files its performance-based formula rate tariff pursuant to subsection (c) of this Section, with what the revenue requirement would have been had the actual cost information for the applicable calendar year been available at the filing date." AG/AARP assert the key to the Commission's correct interpretation of this issue in its May 29 Order in Docket No. 11-0721 is the recognition that the reconciliation rate base should reflect the "actual cost" of investment and the concomitant return owed on that investment throughout the year – not what return would be paid in the last month of the relevant 12-month period. AG/AARP claim plant added into rate base in the month of December is not in service and providing benefit to ratepayers during the first 11 months of the relevant year. AG/AARP contend that ratepayers should not be forced to provide AIC with a windfall by paying a return, as AIC would have it, on these end-of-year amounts, as if the plant represented by these year-end amounts had been in service for the full prior 12-month period.

AG/AARP indicate that AIC claims that had the actual cost information been available at the time of the annual May 1 filing date, the actual information for the calendar year would reflect the year-end rate base. AG/AARP contend that the inception revenue requirement does not represent the final amount of revenues that consumers will provide the utility for the year. AG/AARP say that while using the end-of-year rate base and including the projection of the following year's net plant additions helps to minimizes the expected difference between the reconciliation revenue requirement and the inception revenue requirement, the reconciliation revenue requirement is the final calculation that must necessarily account for actual incurred levels of all cost, including actual expenses throughout the year and actual net investment requiring a return throughout the year. AG/AARP contend the use of an end-of-year rate base (from the former year) in determining the inception revenue requirement is the first step in estimating that year's revenue requirement that will be later subject to reconciliation, but it does not compel the use of an end-of-year rate base in the calculation of the reconciliation. AG/AARP state that the reconciliation revenue requirement and the inception revenue requirement have different functions, use different data sets, and produce different results.

AG/AARP indicate that AIC also points out in support of its position that the statute is clear the reconciliation rely on FERC Form 1 data for the most recent calendar year before the year of the reconciliation filing and not an average calculated using the year before that and that year. AG/AARP maintain that the statute references the need for the reconciliation to reflect what the revenue requirement would have been had the actual cost information for the applicable calendar year been available at the filing date. AG/AARP maintain that principles of fairness and equity dictate the use of an average rate base to most accurately measure AIC's actual invested capital throughout the reconciliation year.

AIC asserts that references to the word "average" in other places in Public Acts 97-0616 and 97-0646 mean that the General Assembly distinguished between whether they intended an "average" to be used for a year and whether they did not. AG/AARP say AIC claims that the absence of the use of the term average in the Act's reconciliation provisions confirms that year-end rate base, not average, must be used for reconciliations. AG/AAPR contend that AIC fails to note that the statute likewise does not state that an end of year rate base be used in the reconciliation. AG/AARP argue that if the General Assembly intended to include only year-end balances in this regard, it would have so stated, but it did not.

AG/AARP indicate that AIC claims that the need to ensure that customer rates are set to recover the costs of plant those customers are benefiting from supports use of a year-end reconciliation rate base. They say AIC compares reconciliation rate-setting with the use of a historical test year in traditional ratemaking, which typically employs a year-end rate base. AG/AARP believe this analogy is inapt for purposes of establishing reconciliation rates.

AG/AARP note that AIC claims that use of an average rate base will reconcile the projected year-end balance for the reconciliation year back to an average balance, resulting in an under-recovery for reconciliation rate base. AG/AARP assert that AIC distorts the purpose of the reconciliation revenue requirement, as envisioned by the General Assembly's plain language of the statute. AG/AARP claim the intent of the reconciliation is to ultimately reconcile the revenue requirement reflected in rates for each calendar year, beginning with the calendar year in which the utility files its performance-based formula rate tariff pursuant to subsection (c), with what the revenue requirement would have been had the actual cost information for the applicable calendar year been available at the filing date. AG/AARP question what is the carrying cost incurred by AIC for its investment in utility plant during the year being reconciled. According to AG/AARP, the reconciliation should reflect the dollar cost to AIC of carrying the net capital investment (the interest on debt plus equity return) necessary to provide delivery services throughout the 12-month period being examined. AG/AARP claim that the dollar amount is the rate of return times the average rate base – not the year-end rate base. AG/AARP argue that use of a year-end rate base for the reconciliation revenue requirement would accept the fallacy that the plant investment listed at year-end had been in service all year long. AG/AARP say that when a utility plant asset is put into service in December of a given year, it does not borrow new money and incur a capital cost on that plant for the whole year.

AIC complains that use of an average rate base halves the plant investment made during the course of the rate year despite the fact that when the reconciliation rates take effect, 100% of the investment was made and will have been providing service for over a year. AG/AARP claim AIC misconstrues the purposes of the reconciliation process, which is to look back at the year in question and determine AIC's actual costs. AG/AARP assert that the revenue requirement reconciliation process required under the Act ensures a complete matching of rate and revenue levels with the cost of actually providing service during that same period and provides for the accrual of interest on any difference between actual costs and allowed revenues. AG/AARP contend that in this context, the reconciliation process is designed to ensure a full matching of revenues with overall actual costs without regard to how rate and revenue levels were initially set. The key question, AG/AARP claim, is whether average or year-end investment levels are most indicative of the utility's actual deployed investment during the reconciliation year. AG/AARP believe Commission adoption of an average reconciliation rate base will ensure that AIC's actual cost of carrying the capital investment made during the year is recovered and that ratepayers do not overcompensate AIC for the capital costs incurred during that relevant reconciliation rate year.

f. CUB Position

CUB states that under the new formula rate plan, there will be a reconciliation case each year to reconcile AIC's projections with that year (and the rates customers have been paying during that time) with actual cost information from that year. CUB believes that the rate base calculation in the reconciliation case should be based on an average rate base for that calendar year, rather than the year-end rate base recommended by AIC. CUB contends that to do otherwise would allow AIC to over-collect from its customers.

According to CUB, the reference in Section 16-108.5(c)(6) of the Act to what the revenue requirement would have been had the actual cost information for the applicable calendar year been available at the filing date suggests the use of an average rate base methodology for measuring AIC's actual results under the reconciliation. CUB says actual cost information for the applicable calendar year would include additions and subtractions from the jurisdictional rate base as they have occurred throughout the year. CUB claims Section 16-108.5(c)(6) specifically says applicable calendar year and a calendar year is a 12-month period starting on January 1 and ending on December 31. For rate base, CUB believes the calendar year should reflect actual additions and retirements that have occurred during the year. CUB says a calendar year runs from January 1 through December 31. In CUB's view if the legislature had intended a year-end rate base, presumably the specification would have been for a "calendar year-end" and not for the "applicable calendar year."

CUB argues that AIC's proposal to use year-end rate base in the reconciliation would result in ratepayers paying more than AIC's actual revenue requirement for the calendar year. CUB states that AIC's rate base grows throughout the year as new plant additions are put into service. According to CUB under the new formula rate structure, unlike a typical historical test year rate case, a reconciliation will measure the utility's actual earnings during each twelve-month calendar year. CUB asserts this proceeding is more in line with a future test-year case, where an average rate base is used, in which the allowed rate base should reflect actual rate base throughout the year. CUB avers that using a year-end rate base under this formula would amount to assuming that every new plant addition, whether put into service on January 1 or December 31, whether used and useful for 365 days or for only one day, was recoverable as if put into service on January 1st.

AIC claims that the statute requires use of a year-end rate base because of a reference to the actual revenue requirement reflected in the FERC Form 1. CUB contends that the "final" FERC Form 1 for the year includes both beginning and end-of-year information for balance sheet accounts, including those accounts that are the primary source of rate base amounts. CUB believes that contrary to AIC's assertions, the reference to the "final" FERC Form 1 of the year actually suggests that an average rate base should be used. CUB also cites the Commission's decision in Docket No. 11-0721 in support of its position. CUB believes no differences exist in this case that should cause the Commission to come to a different conclusion.

According to CUB, AIC makes three assertions to support its position that year-end, rather than average year, rate base should be used for reconciliations: (1) Public Acts 97-0616 and 97-0646 require it; (2) year-end rate base matches customers' rates with the cost of the plant providing them service; and (3) AIC would be adversely impacted by the use of a year-end rate base for reconciliations. CUB maintains that Public Acts 97-0616 and 97-0646 require statutory interpretation to determine whether year-end or average-year rate base should be used for reconciliations, and all other parties agree, as did the Commission in the ComEd Order, that based on the language of the entire statute, average-year rate base is in line with the statute's intent. CUB also maintains that year-end rate base results in AIC over-collecting from its customers, rather than matching costs to actual expenses.

CUB claims the fact that AIC would be "adversely impacted" by use of a year-end rate base by having a small amount of regulatory lag is hardly an adverse outcome. CUB asserts that some level of regulatory lag is inherent in the recovery of costs that are not yet known. CUB says this is in line with the statute, which contemplates some lag involved in the reconciliation process and compensates utilities by allowing them to receive interest. CUB insists that the rate base calculation in the reconciliation case should be based on an average rate base for that calendar year.

CUB states that the Act does not specifically state that either year-end or average rate base should be used in determining the reconciliation revenue requirement, but is specific and consistent that actual cost information for the applicable calendar year must be used. CUB avers that actual cost information for the applicable calendar year would include additions and subtractions from the jurisdictional rate base as they have occurred throughout the year. CUB claims that AIC seeks to overstate its revenue requirement in reconciliations and collect from its ratepayers for a rate base, and a return on that rate base, that is not reflective of the plant actually in service for the entire year. (CUB Reply Brief at 27)

AIC argues that the formula rate process is akin to a historical test year, and thus end-of-year rate base should be used as it is used in historical test year rate cases. CUB says AIC agrees that the formula rate regime is not a test year process. CUB notes there is no reconciliation process in a historical test year regime; if a utility under-collects as a result of rates based on an historical test year, there is no automatic update to ensure full cost recovery. CUB claims that here, not only is there an automatic reconciliation process, but AIC will actually receive compensation in the form of interest for any delay in cost recovery.

According to CUB, the purpose of the formula rate legislation is not to provide a participating utility with the greatest and earliest possible recovery. CUB observes that Public Acts 97-0616 and 97-0646 stated that the General Assembly favored modernization of the State's electric grid, and found that regulatory reform measures that increase predictability, stability, and transparency in the ratemaking process were needed to promote that investment. CUB believes that requiring that rate base be calculated based on average year rate base rather than year-end rate base is predictable, stable and transparent, and ensures that only the utility's actual costs are recovered from ratepayers.

g. Commission Conclusion

As the Commission understands it, IIEC proposes the use of average rate base in all calculations relating to the formula rate while AIC proposes the use of year-end balances in all calculations relating to the formula rate. Staff recommends using year-end rate base balances for setting the future rate component of the formula rate for each year and using the average rate base for the reconciliation component for each year. The remaining parties who address the issue recommend using a year-end rate base for the initial rate base but recommend using average rate base for all subsequent calculations in the formula rates.

The first step in resolving this issue is to recognize the obvious--that the rate setting process put in place by Public Acts 97-0616 and 97-0646 is quite different from the traditional rate setting process known by the Commission. While the Commission understands AIC's attempts to draw analogies between traditional ratemaking test year principles and the formula rate process, the new statutory language clearly prevents complete reliance on traditional methods of setting rates. Although some aspects of traditional ratemaking under Article IX are still applicable, the input data, the formula rate itself, and the reconciliation practice specified in the Act do not fit neatly into the traditional ratemaking paradigm. AIC's reliance on the past use of year-end data in earlier rate cases therefore holds little sway over the Commission.

Each of the parties argues that the new provisions support their position on the use of average versus year-end rate base. While some claim to know what was intended when Public Acts 97-0616 and 97-0646 were enacted, the Commission is not bound by the views of a few as to what the statute requires. The record in this case warrants the finding that the language used in the statute leaves room for interpretation by the Commission.

Among the arguments interpreting the new statutory language is AIC's claim that the use of the word "final" in Section 16-108.5(d)(1) indicates that the legislature intended for the Commission to rely on year-end values taken from FERC Form 1. If the General Assembly had used the term "year-end" there would be no question what was intended. AIC fails to explain why if the General Assembly intended for year-end information it did not simply use that term. Rather, what is meant by "final historical data reflected in . . . FERC Form 1" is subject to more than one interpretation. As pointed out in the record, FERC Form 1 contains plant data as well as other data for both the beginning of the subject year and the end. FERC Form 1 contains "final" data for essentially the entire year.

Similarly, Section 16-108.5(c)(1) states that the performance based formula rate base shall do the following: "Provide for the recovery of the utility's actual costs of delivery services that are prudently incurred and reasonable in amount consistent with Commission practice and law." The Act does not specify exactly how the "actual costs of delivery services" is to be determined. Using year-end rate base would suggest that the rate base value is constant from January through December. If year-end rate base is used, the rates put in place would not reflect the actual costs of delivery services through the entire year since it is understood that rate base will gradually increase as the infrastructure improvements contemplated under Public Acts 97-0616 and 97-0646 are implemented. If, however, an average rate base is used, the rate base for any particular year under the formula rate regimen would theoretically only be accurate around June and July. Neither outcome perfectly reflects a participating utility's rate base. To mitigate such imperfections, however, Public Acts 97-0616 and 97-0646 incorporate a reconciliation with each annual formula rate filing. The reconciliations will address any over- or under-recovery.

Having concluded that the legislature left room for interpretation of Public Acts 97-0616 and 97-0646 and bearing in mind the impact on customers, the Commission finds that for purposes of determining the rate year revenue requirement, year-end rate base should be used. For purposes of determining the reconciliation revenue requirement, average rate base should be used. Calculating the overall revenue requirement for the formula rate each year in this manner reasonably reflects the language of the statute and sufficiently balances the interests of shareholders and customers. Notably, in light of the increasing plant expenditures each year, the legislature arguably created a system under which under-recoveries by the utility will be the norm. Using year-end balances and average balances in this manner will lessen the gap between the values to be reconciled and thereby minimize the reconciled under-recovery each year, to the benefit of customers. Whatever the under-recovered amount is, AIC will earn interest on that amount to the benefit of shareholders. The amount of interest is set forth below. Accordingly, the Commission adopts the proposed use of year-end rate base for purposes of determining the rate year revenue requirement and average rate base for purposes of determining the reconciliation revenue requirement with the knowledge that it will accurately reflect AIC's actual cost of delivery services over the investment period set forth in Public Acts 97-0616 and 97-0646.

7. Interest Rate on Under/Over Collections

a. AIC Position

Section 16-108.5(c) of the Act provides that the formula rate tariff approved by the Commission must provide for an annual reconciliation, with interest. AIC proposes that the carrying cost rate applicable to over- or under-collection amounts determined in a reconciliation proceeding should be equal to the WACC. AIC believes the WACC is the only proposed interest rate that complies with the statute. AIC says the Act directs the Commission to allow a participating utility to recover the full cost of providing delivery services. AIC argues that the WACC, which is what AIC actually pays for capital, is the only interest rate that will fully compensate it for the capital that was employed in the event of under-collection. AIC explains that under Section 16-108.5(c)(2), the formula rate approved by the Commission should reflect the utility's actual capital structure for the applicable calendar year, excluding goodwill. By deeming AIC to have financed this significant portion of its capitalization solely with debt, as all of the other proposals do, AIC avers that these proposals would shift the overall capital structure financing AIC's operations in direct contravention of the Act's directive that the formula rate reflect a utility's actual capital structure, unless shown to be unreasonable or imprudent.

AIC claims the use of a weighted cost of short-term and long-term debt would not compensate AIC for its actual costs of accessing capital in the markets to fund investments required under the statute. AIC says it effectively would require AIC to alter its capital structure to fund reconciliation amounts with a certain mix of debt, irrespective of: the consequences of using only debt on AIC's financial condition and credit ratings; whether such funding is prudent; and whether such funding is practicable. AIC claims that in effect, the parties are arguing that it is imprudent to fund reconciliation amounts – which themselves represent unrecovered costs associated with the incremental investment in plant that the formula rate is supposed to support – with anything other than debt. AIC believes the far more reasonable position is that this investment should be supported by the same mix of capital as other investment.

AIC argues that the other parties' proposals would also violate the requirement in Section 16-108.5(c)(3) that the formula rate include a cost of equity. AIC says that cost is reflected in the WACC. Citing Section 16-108.5(c)(4)(D), AIC states that when the legislature intended for the Commission to apply an interest rate different from the utility's WACC in a specific context, it said so. AIC insists there is no support for the claim that the legislature intended or authorized the Commission to use anything other than the utility's WACC when calculating the financing costs of the reconciliation deferral. While the other parties rely on the Commission's findings in its Order in Docket No. 11-0721, AIC notes that the Commission has since granted rehearing on the reconciliation interest rate issue.

AIC says the other parties base their proposals on a faulty assumption that reconciliation amounts do not represent or require permanent financing, and that they would either displace or require only short-term debt. AIC states that AG/AARP witness Brosch argues that his proposal is necessary to recognize the short-term, working capital nature of reconciliation amounts. AIC contends that reconciliation amounts are not short-term, and under the Commission's rules, working capital is included in rate base at the WACC.

Because short-term debt is debt issued for a period of less than one year, AIC asserts that reconciliation amounts will not be recovered or refunded within one year. AIC says under the protocols laid out in the Act, an under-recovery experienced in Year 1 will be the subject of an update filing in Year 2 and will be reflected in rates in Year 3. AIC contends that any under-recovery in Year 1 will not be fully recovered until the end of Year 3, meaning that the recovery period is two years. AIC says what AG/AARP and

CUB are proposing is that an investment with a life beyond one year be funded with debt issued for less than one year. In AIC's view, the matching they suggest exists between the nature of the investment and the nature of the supporting financing does not exist.

AIC states that working capital is reflected in rate base at the WACC. AIC relates that Part 285 expressly includes both CWC (Section 285.2070) and materials and supplies (Section 285.2075) in rate base, where they are supported by the full capital structure at the WACC. AIC asserts that if AG/AARP believe that the “working capital nature” of reconciliation amounts must be properly reflected in rates, those amounts should be carried at the WACC, just like other working capital items.

If reconciliation amounts only require the use of short-term debt, AIC says the effect on short-term debt will be fully reflected in AIC actual capital structure used for ratemaking purposes under the formula rate tariff. AIC claims it would not be appropriate to both assign some amount of short-term debt exclusively to reconciliation amounts and also reflect it in the capital structure as though it were also supporting rate base generally. AIC says if that short-term debt is also assumed to be assigned to the under-recovered amount specifically, it will be in two places at once – in the capital structure supporting all investment and supporting the under-recovery specifically. AIC argues that the only way to avoid this double-counting of short-term debt is to reflect short-term debt in the actual capital structure and apply the WACC to the reconciliation amount.

AIC also contends that forcing it to take on more debt would tend to make AIC more risky and adversely impact its creditworthiness. According to AIC, to force an increase in debt leverage now may only result in a perception of increased default risk, thereby increasing the cost of any future AIC borrowing. AIC argues that under formula rates, such an impact would negatively affect customers, as they would bear the costs of the relatively higher borrowing rates.

AG/AARP argue that the Commission should adopt either AIC's cost of short-term debt or the hybrid approach from the ComEd docket as the interest rate applicable to reconciliation amounts. AG/AARP’s recommendation is premised on its contention that a reconciliation amount “represents a short-term obligation” because it will be recovered within a year. AIC maintains that reconciliation amounts will not be recovered or refunded within one year. Staff recommends that the Commission adopt an interest rate for reconciliation amounts that is consistent with the “hybrid approach” that the Commission adopted for ComEd in Docket No. 11-0721. AIC says Staff offers no argument in support of the hybrid approach other than a desire for consistency.

AIC finds it odd that AG/AARP contend that the specific sources of financing (short-term debt, common equity, etc.) cannot be traced to their specific uses. AIC finds this odd because it is AIC's point. AIC insists it can not and should not tie a specific cost item to a specific source of financing. According to AIC, this is exactly what AG/AARP state in the paragraph immediately following the argument regarding the inability to trace dollars from financing source to use: “the purpose of the AG/AARP recommendation . . . [is to] encourage Ameren to incrementally finance such balances with short-term debt.” (AIC Reply Brief at 73, citing AG/AARP Initial Brief at 84)

AIC says the only way it can incrementally finance reconciliation amounts with short-term debt, and still recover its actual costs, is assign the short-term debt to the reconciliation amounts and deduct from the capital structure supporting other investments. If the Commission did not deduct them from the capital structure, then AIC says the same dollars of short-term debt would necessarily be in two places at once: financing reconciliation amounts and supporting rate base items. Regardless of whether one accepts that dollars cannot be traced from source to sink, AIC claims it is undeniable that one dollar of capital financing can only support one dollar of capital needs. AIC says if it borrows a dollar on a short-term basis, that borrowed dollar cannot support one dollar of a reconciliation balance and one dollar of rate base. AIC says those two dollars of capital needs require two dollars of financing, not one dollar used twice.

According to AIC, AG/AARP brush aside that concern, citing Mr. Brosch’s testimony that what the Commission is really doing is just setting an interest rate, and not prescribing the use of specific capital for specific purposes. AIC says this makes no sense. AIC states that if the Commission limits AIC’s cost recovery on reconciliation amounts to the cost of short-term debt, the only way that AIC can recover its actual costs, as the Act mandates, is if AIC finances the reconciliation amounts exclusively with short-term debt and that short-term debt is not deemed to also be supporting other investment.

AIC says AG/AARP’s interpretation of the term “interest rate” is far too narrow. AG/AARP suggest that this term excludes reflection of any equity component in the rate applicable to reconciliation amounts. AIC believes the Act is clear that it is entitled to recover its “actual costs.” AIC insists that AG/AARP’s proposed limitation on the meaning of “interest rate” would deny AIC the opportunity to recover its “actual costs” and thereby violate the express terms of the Act.

b. Staff Position

Consistent with Commission practice, Staff’s proposed reconciliation computation on Schedule FR A-4, line 4 used the interest rate on customer deposits approved by the Commission pursuant to Section 280.70(e)(1) rather than the WACC proposed by AIC. Staff noted that when calculating interest on reconciling amounts or balancing factors, the Commission generally uses the interest rate on customer deposits. Staff also recommends the Commission order on this issue be consistent with the ComEd Order. In the ComEd Order, the Commission adopted a hybrid approach to use the weighted costs of short-term debt and long-term debt and exclude the weighted cost of common equity as the methodology in calculating the interest rate. Staff acknowledges that this is still at issue in the rehearing phase of the ComEd proceeding; however, until such a time the Commission issues an order on rehearing that changes this decision, the

Commission conclusions remain in effect and should be consistently applied in this similar proceeding. Staff believes it would be unreasonable for the AIC formula rate, which is based upon the same statute as ComEd's, to contain a different conclusion on the same issue as ruled upon in Docket No. 11-0721.

c. CUB Position

CUB suggests that carrying costs on over-collections by AIC should be computed at the larger of (1) AIC's overall cost of capital or (2) AIC's short-term debt cost. CUB suggests carrying costs on under-collections by AIC should be computed at the smaller of (1) AIC's overall cost of capital or (2) AIC's short-term debt cost. CUB believes this is the fairest scenario for ratepayers: if AIC has over-collected from ratepayers, then it has earned a return on that amount and ratepayers should be refunded at the same interest rate that AIC earned on the over-collected amount. CUB says if AIC has under-collected from ratepayers, AIC should recover only what that under-recovery actually cost AIC if it had to get short-term financing elsewhere to cover the shortfall.

CUB claims it is necessary to use the interest rate/carrying cost proposed by Mr. Smith to protect ratepayers from manipulation of the projected plant addition amounts by AIC. CUB says AIC will be responsible for developing the amount of its projected plant additions for each year and could thus produce over-collections simply by over-projecting such plant additions. CUB asserts that requiring a higher interest rate for over-collections will thus provide an appropriate and necessary deterrent to AIC from making over-projections of plant additions. CUB also claims that allowing interest on under-collections based on the lesser of the short-term debt rate and AIC's overall weighted cost of capital, will also encourage AIC to make accurate projections of plant additions, because its earnings on under-collected balances resulting from misprojecting plant additions would be at the lower of those rates. CUB believes the carrying cost rates proposed by Mr. Smith will protect ratepayers and will provide appropriate compensation to ratepayers from AIC's use of their money in the formula rate plan over-collections.

CUB argues that in the ComEd proceeding, Staff witness Ebrey proposed using the Commission-ordered customer deposit interest rate. CUB suggests that is another reasonable approach to use in calculating the interest rate on under-collections. CUB says If the customer deposit rate is to be used for the reconciliation, the carrying costs on over-collections by AIC should then be computed at the larger of (1) AIC's overall cost of capital or (2) AIC's customer deposit interest rate.

CUB notes that AIC would prefer to use its WACC for both over- and under-collections. CUB claims that approach would unfairly over-compensate AIC by allowing it to recover more than it actually cost to finance a shortfall. CUB says the Act provides for interest to be applied, but does not specify how the interest rate should be determined or whether a different interest rate should be applied to over- and under-collections. According to CUB, AIC relies on the fact that the Act requires that a participating utility shall recover the full cost of providing delivery services, and argues that the WACC, which is what AIC actually pays for capital, is the only interest rate that will fully compensate AIC for capital that was employed in the event of under-collection.

CUB says AIC ignores the fact that in the event that an under-collection occurs and certain capital is employed in the meantime, it does not actually pay its WACC if additional financing is needed. CUB claims any additional financing would be short-term; thus, to be made whole, AIC need only collect its short-term debt rate from customers. In the event of an under-collection, CUB contends that AIC's approach would significantly over-compensate AIC by allowing it to recover more than it actually cost to finance a shortfall. In the event that AIC over-collects from its customers, CUB says AIC does indeed earn its WACC on that over-collection, thus CUB agrees that WACC should be used in that case. CUB states that if AIC has over-collected from ratepayers, then it has earned a return on that amount and ratepayers should be credited at the same interest rate that AIC earned on the over-collected amount.

According to CUB, AIC argues that CUB’s approach would force it to take on more debt, thus making AIC more risky and adversely impacting its creditworthiness. CUB contends that AIC would not be forced to take on more debt to finance a shortfall in the event of an under-collection. CUB says AIC may be able to cover that “shortfall” in any number of ways. CUB’s point is simply that at most, if AIC did have to obtain additional financing to cover a shortfall, financing would be short-term in nature and the interest rate thereon would so reflect. CUB suggests AIC's arguments about its creditworthiness are a strawman, because if it has to seek financing due to an under-collection, the interest rate it collects from customers in a later reconciliation does not make it any more or less true that financing is required at that time.

AIC argues that the short-term debt rate is not appropriate because the administrative code defines short-term debt as debt issued for a period of less than one year, and there is a lag of more than a year from the end of a reconciliation year until the time rates based on that year go into effect. CUB claims the ComEd Order, which included the use of the average test year concept for the reconciliation period, acknowledged that collection or refund of reconciliation balances will be occurring with a one- to two-year lag. CUB contends that reconciliation balance components related to operating and maintenance expenses would appear to entail a period of, at most, two years for full cost recovery or refund. CUB also says the portion of the reconciliation balance related to net projected capital investments would entail a period of approximately one year for full cost recovery or refund. CUB believes AIC's point that the carrying cost rate applicable for reconciling under-collected balances should not be based exclusively on the cost of short-term debt may be valid. CUB says the concept of matching a debt-based interest rate to the recovery period applicable to reconciling balances was recognized by the Commission’s ComEd Order.

For the carrying cost rate for under-collected reconciliation balances for AIC, CUB supports the use of a “hybrid” debt rate that is based on approximately 1/2 short-term debt (for the one-year reconciliation items) and approximately 1/2 year of intermediate-term debt (for the two-year period for the other reconciliation items.) CUB says that is what the Commission used in the ComEd Order. CUB believes the use of a hybrid debt cost rate (for under-collections only) would be appropriate, because it represents an interest rate that is based upon debt that is relevant to AIC for the time duration of the reconciliation. Accordingly, for under-collected reconciliation balances, CUB submits that it would be reasonable to use a hybrid debt-based carrying cost rate, based on an approximately equal blend of short-term (one year) and longer term (ideally, two-year) debt interest rates. CUB states that because two-year debt financing rates are not available in the current AIC formula rate plan record, a simple average of AIC's short and long-term debt cost rates should suffice for the initial reconciliation period carrying cost rate if there was an under-collected reconciliation balance. For the initial reconciliation period, CUB says it appears that AIC has an over-collected balance.

CUB continues to support the use of WACC for overcollected balances. CUB believes this would protect ratepayers from manipulation of the projected plant addition amounts by AIC.

d. AG/AARP Position

AG/AARP state that in contrast to the specific ROE described elsewhere in Section 16-108.5, the drafters of this subsection did not specify the interest rate to apply to the reconciliation amount and did not refer to either the ROE or any other measure of capital cost for this purpose. AG/AARP suggest the Commission must determine the appropriate rate of interest to apply to reconciliation amounts based on the nature of the cost. They relate that the formula prepared by AIC would have consumers pay AIC's WACC on any reconciliation amount. AG/AARP argue that in addition to not being authorized by the statute, which calls for simple "interest," this would result in an excessive interest rate that does not represent the actual cost of incremental new capital needed for the short period of time that the reconciliation amount will be outstanding before its guaranteed recovery under the formula.

AG/AARP indicate that the potential reconciliation amount will not be known until the review of the actual data for the revenue requirement is presented, and will be set for recovery for the next annual rate year. AG/AARP say the known balance will be collected within the year following the determination of the reconciliation amount. AG/AARP contend this represents a short-term obligation (as it can be a credit or a charge). AG/AARP argue that these balances therefore do not require permanent financing by AIC, and should not be expected to require new AIC common stock issuances or parent company equity infusions for financing. They believe there is no basis to assume that incremental equity financing will occur in connection with the annual revenue reconciliations. AG/AARP assert the interest rate on the reconciliation amounts should not be inflated by treating this regulatory asset like longer term assets, as AIC's approach would do.

AG/AARP witness Brosch recommends that a short-term debt interest rate should be used for purposes of reconciliation credits and charges, recognizing AIC's ability to access credit markets at favorable cost rates to finance short-term asset investments. AG/AARP state that the average cost of short-term debt to Ameren was only 2.3% in 2011. AG/AARP suggest an alternative cost rate for consideration is the interest rate AIC currently pays on customer deposit balances, which is presently 0%.

AG/AARP state that short-term debt cost rates have recently remained at historically low levels and tend to be generally lower than the costs of more permanent debt capital most of the time. With the large anticipated infrastructure investments AIC will make pursuant to new Section 16-108.5 and because inflation impacts upon annual operating expenses are not projected beyond test year-end in setting formula rates, AG/AARP suggest it is reasonable to expect future reconciliations to often yield reconciliation balances that are chargeable to ratepayers. Under these circumstances, AG/AARP believe a relatively lower interest rate would be beneficial to ratepayers. AG/AARP note that both Staff and CUB witnesses likewise endorsed use of a short-term debt interest rate on reconciliation balances.

According to AG/AARP, AIC claims it is inappropriate to both assign some amount of short-term debt exclusively to reconciliation amounts and also reflect it in the capital structure as though it were also supporting rate base generally. AG/AARP say the gist of AIC's argument on this point is that it is not appropriate to both assign some short-term debt exclusively to reconciliation amounts and also reflect it in the capital structure as though it were also supporting rate base. AG/AARP believe this concern would only be valid if AIC actually financed regulatory asset amounts resulting from the reconciliation process solely with incremental short-term debt. They assert AIC’s argument on this point wrongly assumes that regulators attempt to directly assign capital to particular investments, which is a false assumption.

AG/AARP note that reconciliation balances can be either positive amounts that require incremental financing until recovered from customers or negative amounts that provide capital from customers until refunded through rates. When combined with other constantly changing elements of working capital, AG/AARP say utility cash flows are dynamic and incremental financing requirements can be met a number of different ways that do not imply any direct assignment or capitalization to particular assets. AG/AARP also say every dollar in AIC's capitalization cannot be sourced to specific rate base or other assets. AG/AARP state that when Ameren Corporation issues common stock and some of the proceeds are invested in AIC, it is not possible to identify the specific assets within its rate base that were financed with that specific equity issuance. According to AG/AARP, it is not possible to know, when one looks at AIC’s cash flow from operations, which specific dollars were re-invested in the business and which dollars were used to pay dividends to Ameren Corporation.

AG/AARP contend the purpose of their recommendation regarding use of a short-term debt cost interest rate on reconciliation balances was to recognize the short-term, working capital nature of such amounts that are pending recovery from or return to ratepayers and to then encourage AIC to incrementally finance such balances with short-term debt, so as to reduce the cost of such financing to the extent possible. AG/AARP suggest if other forms of capital, such as long-term debt, are also assumed to be supportive of reconciliation regulatory asset balances, AIC's concerns about double counting short-term debt are not warranted. Mr. Brosch testified that if specific types of capital are not prescribed by the Commission for financing reconciliation balances, in favor of simply setting a reasonable interest rate for such balances, AIC is free to manage its capital structure decisions without regard to any specific assignments of short-term debt or any other types of capital.

AG/AARP believe AIC has failed to demonstrate that it is appropriate to apply an overall WACC to the reconciliation balance as a carrying charge. They say AIC has not shown, for example, that reconciliation balances would require any new equity financing or other incremental permanent financing by AIC. They also note that the Commission's Order in Docket No. 11-0721 rejected ComEd's request, like AIC's, to approve the utility's WACC to calculate carrying charges on any reconciliation balances.

AG/AARP suggest this "hybrid" approach adopted by the Commission, if also applied to AIC, would avoid AIC's concern regarding an alleged need to specifically assign and track incremental short-term debt associated with reconciliation balances. AG/AARP believe either the Brosch-recommended short-term interest rate or the hybrid approach endorsed by the Commission in the ComEd formula rate case should be applied to any reconciliation balances (and credits) calculated each year under the reconciliation process envisioned in Section 16-108.5 of the Act.

In addition to applying a short-term debt rate to any reconciliation balances (or credits), or the use of a hybrid interest rate approach as recently approved by the Commission, AG/AARP note that Mr. Brosch also proposed the use of an alternative accounting measure that could appropriately be employed to determine the interest cost applicable to revenue requirement reconciliation variances. AG/AARP suggest the Commission could deem the revenue requirement variances under formula ratemaking to be regulatory assets that represent a deferral of operating expenses to be recoverable (or returnable) in future rate periods. Since operating expenses are income tax deductible when incurred by the taxpayer, AG/AARP say the deferred income tax balances associated with such expense deferrals could be used to reduce the balance upon which interest is accrued. AG/AARP say application of interest to only the net of income tax balance associated with such deferrals is consistent with the economic reality that income tax savings would be realized from AIC's delayed recovery of tax deductible expenses and would serve to reduce the overall interest burden upon ratepayers by about 40%.

According to AG/AARP, AIC's argument is rooted in its claim that Section 16-108.5(c) requires that the utility recover actual costs of delivery services, thereby demanding in place of an interest rate the use of the WACC which is what AIC actually pays for capital. AG/AARP assert that AIC selectively distorts the plain language of the statute noting that Section 16-108.5(c) states simply that the formula rate tariff must provide for an annual reconciliation, with interest. AG/AARP claim that in contrast to the specific ROE described elsewhere in Section 16-108.5, the drafters of this subsection 16-108.5(d) did not specify the interest rate to apply to the reconciliation amount and did not refer to either the ROE or any other measure of the utility's embedded capital costs for this purpose.

AG/AARP state that AIC argues that the WACC is the only interest rate in line with the Act's directives regarding rate of return and capital structure, citing Section 16-108.5(c)(2). AG/AARP contend that when speaking about the reconciliation interest rate to be applied to reconciliation balances, the General Assembly included no such language. AIC claims that the use of a weighted cost of short-term and long-term debt would not compensate AIC for its actual costs of accessing capital in the markets to fund investments required under the statute. They say AIC never claimed, let alone proved that it would, in fact, head to the capital markets to fund investments required under the statute. AG/AARP note that WACC is reflective of all of its historical financing activities and contend it is not indicative of the incremental cost of new capital AIC may incur to finance any future reconciliation balances.

According to AG/AARP, AIC argues that the specific reference to application of a debt-only return on a pension asset at Section 16-108.5(c)(4)(D) means that whenever the legislature intended for the Commission to apply an interest rate different from the utility's WACC in a specific context, it said so. AG/AARP claim this argument presumes that the reconciliation "interest" reference in Section 16-108.5(d) that the "reconciliation shall be reflected as a credit against, or recovered as an additional charge to, respectively, with interest, the charges for the applicable rate year" equates with language in Section 16-108.5(c)(3) that the formula rate itself shall "include a cost of equity . . . ." In AG/AARP's view, this brand of statutory interpretation cannot be harmonized with the actual language of Section 16-108.5(d).

AG/AARP state under the well-established rules of statutory construction, the words used in a statute must be given their ordinary and popularly understood meaning, and the relevant language must be read within the context of the entire provision of which it forms an integral part. They say that here, the General Assembly required the application of "interest" to reconciliation balances, not the utility's WACC. AG/AARP believe that establishing what is a reasonable interest rate is within the province of the Commission.

AG/AARP note that AIC argues that reconciliation amounts are not short-term debt and under the Commission's rules, short-term debt is issued for a period of less than one year, citing Section 285.115. AG/AARP say AIC contends that because reconciliation amounts covering Year 1 will be the subject of an update filing in Year 2 and will be reflected in rates in Year 3, the recovery period should be assessed as a two-year period. They also say AIC compares the reconciliation interest amount to CWC and materials and supplies, which are included in rate base at the WACC.

AG/AARP argue that AIC ignores the plain language of the statute. AG/AARP say CWC and materials and supplies investments are included in a utility's rate base under the Part 285 rules, but reconciliation amounts are not included in rate base. According to AG/AARP, the statute instead requires the utility to separately accrue a rate of interest to reconciliation amounts that are then to be included within the revenue requirement approved by the Commission. AG/AARP claim AIC's references to CWC and materials and supplies, which are rate base assets, is misplaced.

AG/AARP maintain that reconciliation interest should represent some reasonable estimate of what it costs the utility to finance marginal or incremental new capital requirements. They believe the relevant cost measure is not the utility's embedded capital costs, such as the WACC, which includes the cost of long-term debt and equity for all the prior years in which debt was issued and is still outstanding. AG/AARP claim the use of a short-term debt (or even the Commission-ordered hybrid amount) reflects the fact that the reconciliation balances can be either positive amounts that require incremental financing until recovered from customers or negative amounts that provide capital from customers until refunded through rates.

AIC opines that it would not be appropriate to both assign some amount of short-term debt exclusively to reconciliation amounts and also reflect it in the capital structure as though it were also supporting rate base generally, calling the proposal a double-counting of short-term debt. According to AG/AARP this concern would only be valid if AIC actually financed regulatory asset amounts resulting from the reconciliation process solely with incremental short-term debt. They believe AIC's argument on this point wrongly assumes that regulators attempt to directly assign capital to particular investments, which is a false assumption.

e. IIEC Position

IIEC supports the essence of the positions of Staff and AG-AARP, that the interest rates on any annual reconciliation adjustments under the formula rate should reflect short term borrowing costs.

f. Commission Conclusion

Section 16-108.5(d)(1) of the Public Utilities Act reads, in relevant part, as follows:

> (1) The inputs to the performance-based formula rate for the applicable rate year shall be based on final historical data reflected in the utility's most recently filed annual FERC Form 1 plus projected plant additions and correspondingly updated depreciation reserve and expense for the calendar year in which the inputs are filed. The filing shall also include a reconciliation of the revenue requirement that was in effect for the prior rate year (as set by the cost inputs for the prior rate year) with the actual revenue requirement for the prior rate year (as reflected in the applicable FERC Form 1 that reports the actual costs for the prior rate year). Any over-collection or under-collection indicated by such reconciliation shall be

> reflected as a credit against, or recovered as an additional charge to, respectively, with interest, the charges for the applicable rate year.

(emphasis added). AIC believes the weighted average cost of capital (WACC) is the only proposed interest rate that complies with the statute, while Staff and intervenors argue a variety of methodologies based on short-term debt costs, the customer deposit rate, the Commission's "hybrid" approach from Docket No. 11-0721, and blends of these approaches based on whether the balance has been over- or under-collected.

The Commission first addresses whether the intent of the General Assembly is clear from the Act regarding what manner of calculating "interest" should apply. AIC contends that WACC is the only rate of interest that complies with the statute. A plain reading of Section 16-108.5 reveals that the General Assembly chose to use the term "investment return" when a participating utility's WACC was intended.[4] While this may not be determinative as to what specific method of computing interest is appropriate, it is determinative in ascertaining whether using WACC for reconciliation balances was the clear intent of the legislature, as AIC contends it was. Should the General Assembly have intended for the reconciliation balance's interest rate to reflect the utility's WACC, the legislature demonstrated clear understanding of how to make that intent known. Instead, it chose simply to state that the balance would be recovered "with interest."

Given this limited statutory guidance, the General Assembly left it to the Commission to determine what constitutes an appropriate rate of interest for any over-collection or under-collection of the reconciliation balance. Finding limited guidance in the governing law, the Commission now turns to the proposals of the parties in record evidence. AIC, as set forth above, argues that WACC constitutes the appropriate rate of interest. Staff believes the interest rate for the AIC formula rate should be consistent with the conclusion in Docket No. 11-0721 for ComEd. CUB recommends that carrying costs on under-collections by AIC should be computed at the smaller of (1) AIC's overall cost of capital or (2) AIC's short-term debt cost. AG/AARP recommend that a short-term debt interest rate should be used for purposes of reconciliation credits and charges, recognizing AIC's ability to access credit markets at favorable cost rates to finance short-term asset investments. AG/AARP state that the average cost of short-term debt to Ameren was 2.3% in 2011. AG/AARP also suggest an alternative cost rate for consideration is the interest rate AIC currently pays on customer deposit balances, which is presently 0%. The Commission examines each of these various proposals below.

Starting with WACC, the Commission believes WACC is an inappropriate interest rate for reconciliation balances because, as a threshold matter, WACC has not

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[4] Specifically, Section 16-108.5(c)(4)(D) provides in relevant part as follows:

(4) Permit and set forth protocols, subject to a determination of prudence and reasonableness consistent with Commission practice and law, for the following:

> (D) investment return on pension assets net of deferred tax benefits equal to the utility's long-term debt cost of capital as of the end of the applicable calendar year;

traditionally been applied as such.[5] As WACC draws upon long-term debt and equity in its calculation, WACC cannot reflect the true incremental cost or credit of any 16-108.5 reconciliation balance. The potential reconciliation amount will not be known until the review of the actual data for the revenue requirement is presented, and will be set for recovery for the next annual rate year. As such, the known balance will be collected within the year following the determination of the reconciliation amount. This represents a short term obligation (as it can be a credit or a charge). These balances therefore do not require permanent financing by Ameren, and should not be expected to require new Ameren common stock issuances or parent company equity infusions for financing. Reconciliation balances can and should be incrementally financed. The Commission finds that the interest rate on the reconciliation amounts should not be inflated by treating this regulatory asset like longer term assets, as the choice of WACC would do. Thus, the Commission, after giving due consideration, declines to adopt WACC as the interest rate for reconciliation balances, as AIC suggests, or for only over-collection balances, as CUB suggests.

Staff recommends that the Commission adopt an approach similar to the conclusion reached in Docket No. 11-0721, ComEd's initial formula rate case under Section 16-108.5. The approach taken in that docket calculates the reconciliation balance interest rate by averaging the weighted costs of short-term debt and long-term debt and excluding the weighted cost of common equity. While the Commission appreciates the need for consistency in statutory interpretation, the Commission notes that this issue is currently on rehearing in Docket No. 11-0721 to revisit, in part, that very conclusion. The challenges of giving proper interpretation to Section 16-108.5 are still, essentially, being worked through by the Commission for the first time, and the Commission's primary concern remains determining its conclusions based upon the proposal best-supported by the governing law and record evidence. Should the Commission see errors in its prior determinations, it has both the will and power to correct them.

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[5] Other references to retroactive adjustments of rates "with interest" appear throughout the Public Utilities Act, and the Commission has never interpreted these provisions as permitting a rate of interest equal to a utility's WACC. *See, e.g.,* Section 8-306(k) ("When the customer is due a refund resulting from payment of an overcharge, the utility shall credit the customer in the amount of overpayment *with interest* from the date of overpayment by the customer. The rate for *interest* shall be at the appropriate rate determined by the Commission under 83 Ill. Adm. Code 280.70." [emphasis added]). Section 9-252 (Complaint made to ICC for improper charge) ("When complaint is made to the Commission concerning any rate or other charge of any public utility and the Commission finds, after a hearing that the public utility has charged an excessive or unjustly discriminatory for its product, commodity or service, the Commission may order that the public utility make due reparation to the complainant therefore, *with interest* at the legal rate from the date of payment of such excessive or unjustly discriminatory amount." [emphasis added]); 9-252.1 (Billing errors) ("When a customer pays a bill as submitted by a public utility and the billing is later found to be incorrect due to an error either in charging more than the published rate or in measuring the quantity or volume of service provided, the utility shall refund the overcharge *with interest* from the date of overpayment at the legal rate or at a rate prescribed by rule of the Commission." [emphasis added]). All of these provisions, which reference the awarding of refunds with interest, are designed to make the customer whole for excess revenues collected during a designated period, similar to the reconciliation provisions of Section 16-108.5 of the Act. At no time in the awarding of refunds with interest under these provisions has the Commission established a rate of interest at the utility's WACC.

Upon consideration, the Commission believes the methodology used in 11-0721 to be flawed and rejects its adoption. Not only may long-term debt be inappropriate to include in an interest rate calculation based on the nature of the reconciliation balance being financed, but the weight given to each component of the Company's capital structure is informed by concerns pertinent to its entire rate base, and not merely unique to the reconciliation balance. These weights are also informed by the weight given to Ameren's common equity, and as set forth above, the Commission believes that should not be expected to require new Ameren common stock issuances or parent company equity infusions for financing its reconciliation balance. While the resulting interest rate does provide an attractive midpoint between AIC's WACC proposal and intervenors' customer deposit rate proposal, the Commission declines to adopt a methodology based simply on the outcome of present inputs and believes that the methodology adopted must stand as defensible on its own terms. Simply blending the company's short-term and long-term debt using weighting borrowed from a separate context is not a sound methodology for determining the interest rate. The Commission declines to adopt this approach.

Other parties have proposed that the Commission calculate the interest rate for reconciliation balances at the customer deposit rate. It seems to the Commission that the primary justifications for this proposal are fairness and symmetry. However, the Commission believes that reconciliation interest rate should strive to represent some reasonable estimate of what it costs the utility to finance marginal or incremental new capital requirements. The methodology for calculating the customer deposit rate was developed in a separate proceeding that was informed by a separate record, and therefore there is no evidence that the customer deposit rate corresponds with any estimate of the costs at issue in this proceeding. Thus, the Commission declines to adopt this approach.

AG/AARP witness Brosch recommends that a short term debt interest rate should be used for purposes of reconciliation credits and charges, recognizing Ameren's ability to access credit markets at favorable cost rates to finance short term asset investments. For example, the average cost of short term debt to Ameren Corporation was 2.3% in 2011. Mr. Brosch noted that short term debt cost rates have recently remained at historically low levels and tend to be generally lower than the costs of more permanent debt capital most of the time.

The Commission adopts the recommendation of AG/AARP to apply a short term debt cost rate as the reconciliation interest rate. This rate fairly compensates either the Company or customers for the potential lag in recovery of actual costs that exceed (for the Company) or lag (for the customer) the revenue requirement established in annual formula rate proceedings for the relevant 12-month period. This will ensure that neither ratepayers nor the Company pay more than the Company's actual costs/benefits of carrying a reconciliation balance. Of the proposals in record evidence, the Commission believes that short term debt best matches with the actual incremental cost of any reconciliation balance. It is therefore adopted.

8. Consistency with ComEd Formula Rate Tariff

a. IIEC Position

According to IIEC, the Commission made certain modifications to the ComEd formula rate which should also be made in the context of the AIC formula rate. IIEC says the ComEd modifications included a directive from the Commission that ComEd identify separately on its Schedule FRA-1 of its formula rate the effects of the earnings collar described in Section 16-108.5 of the Act. IIEC says that the earnings collar permits AIC to vary by 50 basis points above or 50 basis points below the return on common equity established pursuant to the formula described in the statute. IIEC states that currently, AIC's proposed Rate MAP-P includes its earnings collar adjustment on its Schedule FRA-1 Rec line 23. IIEC believes the earnings collar adjustment should be stated on AIC's revenue requirement schedule or Schedule FRA-1 in an additional line below the proposed line 23, "Reconciliation of Prior Year." IIEC recommends that, as it did in the ComEd proceeding, the Commission should order AIC to separately state the earnings collar calculation and the results of the collar allocation in Rate MAP-P.

IIEC states that under Section 16-108.5(g), AIC is required to report to the Commission by July 31, 2014, its average annual rate increases for residential customers, on a per kWh basis, over the previous three years. IIEC says an annual rate increase of 2.5% per year would disqualify AIC from use of the formula rate mechanism. IIEC claims AIC has signaled its preference for formula rates by filing this case. According to IIEC, the required determination and report of a rate increase in per kWh charges can be directly affected by the starting point for the year-to-year comparisons. IIEC says AIC has not advised the Commission of the starting point it plans to use in computing that performance benchmark. IIEC proposes, consistent with the decision in Docket No. 11-0721, that the Commission determine and advise all parties of the starting point for that three year assessment. IIEC believes the starting point should be the rates ordered by the Commission in AIC's last electric rate case, Docket Nos. 09-0306 et al. (Cons.), adjusted for the cost of equity, as determined by the current statutory formula. AIC says the Commission adopted IIEC's recommendation in ComEd's formula rate case. IIEC suggests that to ensure consistency between the formula rate approach adopted for ComEd and the formula rate approach for AIC, the Commission should impose the same requirement on AIC here.

IIEC also states that AIC should be directed, as ComEd has been, to provide relevant Parts 285 and 286 information with its formula rate filings.

b. AIC Position

With regard to IIEC's three proposals raised in its Initial Brief, AIC states that if these were IIEC proposals in the ComEd case, which was filed over two months before the AIC case, then IIEC clearly knew about them before the time of its Initial Brief. AIC says IIEC never mentioned these proposals in any of its testimony in this case and never asked any witness about them at hearing. AIC asserts that there are rounds of testimony for a reason: so that the Commission can receive evidence in an orderly fashion, in which parties submit testimony and other evidence pertaining to the issues in dispute. AIC does not contend that legal issues must be disclosed in testimony, but asserts that policy and tariff operation issues such as those raised by IIEC are precisely of the type that benefit from explanation and debate in testimony by qualified witnesses. AIC says conjecture of counsel in a brief is no substitute. AIC recommends that IIEC's proposals be rejected, and IIEC should be directed to cooperate in the orderly development of the record and the briefs in future proceedings.

c. Commission Conclusion

The Commission is concerned that IIEC did not properly, within the context of the appropriate confines of the record in this matter, make its recommendation that the formula ratemaking process and the formula rates for Ameren and Commonwealth Edison Company be made consistent. Specifically, IIEC's recommendation appears for the first time in its Initial Brief and requests that the Commission require the inclusion of the earnings collar calculation in Schedule FR A-3 of Ameren's formula rate, the identification of the starting point for the calculation of the annual cents per kWh increase for residential customers, or the filing of relevant schedules from Parts 285 and 286 of the Commission's rules on standard rate case filing requirements. Such a situation has not permitted the Commission the opportunity to have a fully developed record on this matter and has foreclosed potentially necessary evidentiary support and position statements from the parties on this point. Indeed, Section 10-103 of the Act is quite clear on the Commission's adherence to determinations that are bound by the record:

> In all proceedings, investigations or hearings conducted by the Commission, except in the disposition of matters which the Commission is authorized to entertain or dispose of on an ex parte basis, any finding, decision or order made by the Commission shall be based exclusively on the record for decision in the case, which shall include only the transcript of testimony and exhibits together with all papers and requests filed in the proceeding, including, in contested cases, the documents and information described in Section 10-35 of the Illinois Administrative Procedure Act.

The Commission recognizes, however, that ultimately it has the obligation to investigate and regulate utilities and may not rely on intervening parties to contest or challenge the evidence offered by the utility. *Hartigan v. Illinois Commerce Comm'n*, 117 Ill. 2d 120, 135. With that said proceedings at the Commission travel a rigorous path which includes the complete examination of issues presented in the docket. Participation of the parties is critical to the development of a full record and does indeed require that arguments pro or con to the Petitioner's filing be presented in a timely fashion. In this instance, IIEC did not raise its position until the filing of Initial Briefs after the evidentiary record was closed.

While the Commission does not sanction such a disregard for the proper manner of inclusion of an issue in the record of this case, in this instance it appears there is no opposition to the proposal and no party is disadvantaged by consideration of it. A review of the record discloses that Ameren has in fact presented testimony in this case indicating it is reasonable that the two utility formula rates should, where possible, be consistent. The Commission finds it appropriate that there be consistency between the two utilities in Illinois that are filing tariffs under the EIMA formula rate option. Consistent with the determination in the ComEd Order in Docket 11-0721, AIC is directed to include in its formula rate filing the following: the earnings collar calculation in Schedule FR A-3, the starting point for the calculation of the annual cents per kWh for residential rate increases, and the relevant schedules from Parts 285 and 286.

XI. OTHER

A. Original Cost Determination

AIC requested the Commission approve an original cost of electric plant in service as of December 31, 2010, before adjustments for projected plant additions, of $4,908,210,000. Staff recommends the Commission approve AIC's request for an original cost finding. Staff also requests that if the Commission makes any additional adjustments to plant, those adjustments should also be reflected in the original cost determination. Therefore, Staff recommends the Commission include the following language in the Findings and Orderings paragraphs of its order in this proceeding:

> the Commission, based on AIC’s proposed original cost of plant in service as of December 31, 2010, before adjustments, of $4,920,009,000, and reflecting the Commission’s determination adjusting that figure, unconditionally approves $4,908,210,000 as the composite original cost of jurisdictional distribution services plant in service as of December 31, 2010.

AIC does not oppose the inclusion of this language in the order in this case. The Commission finds the proposal regarding original cost determination to be reasonable and it is adopted.

B. Uncollectibles Expense – Net Write-Off in Rider EUA

Staff witness Hathhorn notes that the Commission ordered AIC to change its method of accounting for uncollectibles expense in its gas uncollectible adjustment rider (“Rider GUA”) to the net write-off method in its last gas rate order. AIC says no such ruling was made for its electric uncollectible adjustment rider (“Rider EUA”) since the case was dismissed. As a result, AIC uses two different methods for measuring uncollectibles expense between its gas and electric riders. Staff asserts the formula rate adds further complexity to the recovery of uncollectibles expense so that no more and no less than the actual uncollectible expense is collected. Staff recommends the

Commission order AIC to change its accounting of uncollectibles expense to the net write-off method in Rider EUA. Further, Staff recommends that if AIC agrees, it should provide a revised Rider EUA in legislative language style as part of its rebuttal testimony in this case. AIC agrees that it is reasonable that both the electric and gas uncollectible riders should operate identically in this regard. Additionally, AIC proposes that compliance Rider EUA tariff sheets be filed pursuant to the order in this proceeding.

AIC adds that there are some issues with converting Rider EUA to the net-write off method. Just as it experienced with the recent compliance filing for Rider GUA, AIC states that converting from Account 904 to a net write-off basis must be effective at the beginning of the first full calendar year after the new rates in such proceeding are first placed in effect and an adjustment shall be made, if necessary, to ensure the change does not result in double-recovery or unrecovered uncollectible amounts for any year. AIC indicates that rates from this proceeding will take effect in October 2012, so the first full calendar year following would be 2013. AIC says the gas Rider GUA will begin reconciling to net write-offs beginning with the 2013 calendar year. Thus, AIC says the first Rider EUA incremental adjustment amounts reflecting a net write-off basis would be filed in May 2014 for factors effective from June 2014 through May 2015, reflecting the difference between net write-offs and the uncollectible expense amount included in rates for 2013. According to AIC, the proposed Rider EUA reflects these modifications.

It appears to the Commission that Staff and AIC are in agreement regarding this issue. The Commission believes that their agreement constitutes a reasonable resolution and adopts it.

C. Net Plant Allocator

Staff recommends that AIC correct its formula rate, specifically AIC Ex. 2.1, Schedule FR A-2, line 18, for an error in the Excel spreadsheet. Staff witness Hathhorn notes that the cell in question in Column C does not contain the formula as indicated in Column B. AIC says this correction created a small change to the Net Plant Allocator on line 20, from 82.89% to 82.87%. AIC explains that the formula correction made on AIC Ex. 13.1, Sch FR A-2, line 18, changed the amount shown from (9,556) to (9,083), changed the calculated amount shown on line 19 from 2,638,953 to 2,638,480, and changed the Net Plant Allocator percentage shown on line 20 from 82.89% to 82.87%. It appears that Staff and AIC currently agree regarding the net plant allocator and the Commission adopts this allocator for purposes of this proceeding.

D. Depreciation Study

Staff witness Everson recommends that AIC update its electric depreciation rates and reflect them in its next formula rate filing or its next general rate case, if a formula rate filing is not utilized. Staff further recommends that the updated depreciation rates be based on an updated depreciation study. AIC says it is in the process of preparing a depreciation study currently with the intent of including the results of that study in its depreciation rates beginning January 2013. AIC also intends to provide the results of the study with evidence submitted in its May 2013 formula rate filing. The Commission hereby directs AIC to provide an updated electric depreciation study and to provide the study and the results from the study in its next formula rate filing or its next general electric rate case.

E. Rate Case Expense – Section 9-229 Statement

AIC states that it has not requested recovery of rate case expense related to this proceeding as none were incurred in 2010. AIC says it will request recovery of these expenses in future filings as costs are incurred. The language of Section 9-229 of the Act requires the Commission to expressly address the justness and reasonableness of any amount expended by a public utility to compensate attorneys or technical experts to prepare and litigate a general rate case filing. Given the requirement for the Commission to expressly address this issue in its order, Staff recommends, and AIC concurs, that the Commission incorporate the following language into its rate order in this proceeding:

> Pursuant to Section 9-229, the Commission is required to expressly address in its final order the justness and reasonableness of any amount expended by a public utility to compensate attorneys or technical experts to prepare and litigate a general rate case filing. The costs included for recovery in this filing are amortization of costs approved in Docket No. 04-0294, 07-0585 et al (Cons.), and 09-0306 et al (Cons.) that were previously established as regulatory assets by the Commission in that order. The costs associated with this proceeding were not incurred in 2010 and as such, are not considered for recovery in this proceeding. Costs incurred in 2011 and 2012 that are related to this proceeding will be considered as part of the proceedings related to the recovery of costs for those years. Thus, there are no costs expended by the Company to compensate attorneys or technical experts to prepare and litigate a general rate case filing for the Commission to address in this proceeding.

The Commission finds the agreement between Staff and AIC regarding rate case expense to be reasonable and it is hereby adopted.

F. CUB Recommendations for Improvement

1. CUB Position

CUB asserts that under the Act, the Commission has an opportunity to improve the electric industry's performance in terms of both innovation and cost-effectiveness. According to CUB, the Commission has an ongoing responsibility to ensure utility investments are prudent and reasonable before any cost recovery is allowed from ratepayers. CUB states that the Act requires AIC to spend an “estimated” $625 million above average capital spending for 2008-2010. CUB says AIC has already made adjustments to its planned plant investment, adjusting its budgeted plant additions in developing its proposed rate base in this case. CUB contends that the Act presents a unique challenge to the Commission because it divorces the Commission's review of major investments in infrastructure and new technologies from its review of AIC's revenue requirement from those investments. CUB claims AIC could over-spend and over-hire to meet its statutory obligations as a participating utility.

CUB states that inherent in any utility expenditure are the following risks: (1) the project will end up more costly than expected; (2) the project will be completed later than expected, pushing the benefits further into the future (thus reducing its value to those who pay up front); (3) the project will produce fewer benefits than expected; (4) the need for the project will disappear, leaving someone —customers or investors– responsible for the sunk cost; and (5) an alternative solution, ruled out or unknown initially, turns out to be more cost effective than the expenditure. CUB claims the Act exacerbates these risks by authorizing the utility to seek prudence decisions prior to expenditures, putting the Commission at risk of approving actions without having a clear vision and perspective. CUB suggests, for example, since the formula rate process invites the utility to obtain regulatory approvals pre-expenditure, AIC has an incentive to underestimate its costs to win a finding of prudence for a particular option. The Commission, CUB says, can become drawn into approving a series of small commitments in the form of annual budgets, leading to upward adjustments as costs exceed estimates. Once the Commission is committed to a given option, CUB claims it could be committed until sunk costs pass the "point of no return," that is, where it no longer makes economic sense to change course because the incremental cost of completing the initial work is less than the total cost of a not-yet started alternative regardless of which alternative actually would have cost less. CUB says that conversely, there is a risk involved with the potential over-estimation of costs, where a utility might assert prudence on completing the project under budget when the prudent level might have been even lower. CUB contends that approvals made without full perspective are risky, opening the door to utility investments which do not maximize the utility's use of ratepayer dollars.

CUB suggests the Commission can mitigate these risks by viewing utility filings under the Act as a whole. CUB claims the central purpose of Commission regulation should be to motivate the utility to excel (i.e., operate efficiently) and to penalize the utility for poor performance. CUB defines "efficient" using an economic perspective: the goal should be to leave no benefits on the table or to forego actions that could make someone better off while making no one worse off. To achieve this result, CUB recommends that the Commission establish the following requirements for AIC's formula rate filings under the Act:

- Require each cost proposal to state all costs, and the expected benefits, and require the utility to commit to achieving those benefits.
- Approve expenditure levels based on the costs of the best available performer, which is not necessarily AIC.
- Approve a project as "prudent" only after gaining the necessary time perspective.

- Using long-term planning, require AIC to connect proposed expenditures to projects that promise benefits, to avoid piecemeal approval of major, long-term capital investments.
- Establish ongoing monitoring – not merely annual, post-hoc reviews— to ensure that project decisions can change as facts change.

CUB alleges that AIC's informational advantage makes it best able to assess risk and an investment lacking shareholder support is unlikely to be prudent. CUB suggests that where AIC seeks to justify an expenditure proposal based on benefits it predicts, and it controls the information supporting its prediction, it must commit to those benefits if it also wants the associated profit. CUB also says that the pre-approved cost recovery must be subject to refund to the extent asserted benefits do not materialize.

CUB suggests the Commission should require any request by AIC for pre-approval of an action or expenditure to include an explanation of the project's total costs and compare those costs to the costs of viable alternative solutions, including any efforts to cap vendor costs. According to CUB, the utility should disclose all risks – all plausible reasons why outcomes could vary from the expected – in a timely fashion so that the Commission can allocate them consistently with economic efficiency. Absent this requirement, CUB claims ratepayer representatives and Staff must guess, because they lack the inside information and expertise controlled by the utility, despite having paid for them through their rates, about possible negative outcomes. CUB says these guesses are then often criticized as “speculative” when they would be unnecessary if the utility disclosed them properly.

In CUB's view, the ultimate goal should be to encourage AIC to find the best performer for the many significant actions and expenditures required of it as a participating utility under the Act. CUB states that while it is not the Commission's role to dictate which contractors and subcontractors AIC should use, it is the Commission's role to base cost recovery on the standards of prudence and reasonableness, which imply using the most cost effective means. CUB says AIC has the burden of proving that its proposed costs are the most effective alternative.

CUB believes the Commission should require AIC to provide all information the Commission needs to determine that the utility’s proposed alternative is the best alternative available. CUB claims AIC’s FERC Form 1 data and any associated workpapers are only a fraction of that necessary information. CUB says the Commission also must require AIC to provide data on how the best performing utilities carry out similar actions and how the utility intends to replicate those actions.

CUB argues that AIC’s control and mastery of inside information gives it more knowledge about what the risks are and what can go wrong. CUB asserts that a prudence review’s quality depends on its timing. CUB contends that post-expenditure facts, like a major cost overrun, stimulate more scrutiny, and the Commission can use a prudence review to determine what went wrong, for what reason, and who was responsible. CUB states that intensity of effort cannot easily occur at the front end, when the adverse outcomes are only possibilities that are easily ignored, downplayed, missed, or dismissed by project proponents as "speculative" or oppositional.

CUB suggests that even when "approving" an action, therefore, the Commission should reserve its power to determine the prudence of the associated cost when it has full perspective. CUB says the Commission can do this by requiring AIC to provide comparative analyses with all relevant alternative expenditures (including a no-expenditure option) for its particular investment proposals. CUB claims the Commission can then determine whether the end result is a decision that a reasonable person would be expected to exercise under the same circumstances encountered by AIC's management.

CUB asserts that to be prudent and reasonable, an expenditure must be the lowest-feasible cost means of achieving a prudent objective, based on the facts known at the time of the decision. Where a specific expenditure is part of a larger project, CUB claims the prudence of the specific expenditure depends on the prudence of the larger picture. To receive approval, CUB contends AIC must prove the prudence of associated projects and show that the total cost of that project compares favorably to feasible alternatives. Absent this demonstration of context and comparison, the Commission risks being drawn into an assembly line of approvals of input costs and actual costs that obscures the vision needed to determine if the projects make economic sense. CUB claims no utility project is done in isolation, and the magnitude of investments contemplated by the Act illustrate how important it is that each expenditure be part of a system of generation and transmission procurement, distribution operations, and customer behavior that causes supply to meet demand cost-effectively. CUB argues that without clear plans, there is no context, no way to distinguish a project that AIC seeks to advance its pecuniary objectives from a project that will address the public's priority needs cost-effectively.

CUB says the Commission also must be prepared for the ongoing monitoring of these expenditures. CUB asserts that any approval of an action or cost rests on assumptions about facts, comparing the predicted costs of the chosen alternative to the rejected alternatives. CUB says the Commission and AIC must be ready to recognize change, acknowledge past error, and shift to the best alternative. CUB believes AIC's proposals for project approvals should include a schedule for periodic, objective re-evaluations that offer opportunities for competitive alternatives to emerge and penalties if the utility withholds or delays the transfer of information relevant to Commission review.

CUB says it agrees with AIC that the Commission retains its substantial authority to determine the prudence and reasonableness of expenditures under Section 16-108.5 of the Act. CUB argues that far from creating new regulatory infrastructure separate and apart from the Act, its proposal provides specific criteria the Commission can use in reviewing AIC's proposed expenditures. CUB claims the additional criteria proposed here would not frustrate the intent of the legislature to spur investments and job creation that will help Illinois' economy. CUB asserts that its proposed criteria are the best way to ensure that the legislature's vision for how the Act will transform Illinois becomes reality. According to CUB, the legislature intended to condition the massive utility investment on providing equally significant benefits to ratepayers. CUB contends the Act's strong emphasis on utility performance, on creating new investment opportunities, and on integrating new grid resources, such as distributed generation and net metering, makes clear that the Commission has a role to play in making sure that this new structure provides benefits to customers.

CUB claims its point is not to rewrite the Act but to show how the Commission can work within the framework of the Act to ensure these long-term and large-scale investments will achieve the benefits, both monetarily and operationally, the Act promises to AIC's customers. CUB contends that it should be presumed that the legislature had a definite purpose in enacting a statute and drafted it so that each part would be in harmony with that purpose and, thus, the general purpose of the whole act controls and all parts are interpreted consistently with that purpose. CUB asserts that taken as a whole, the Act offers a new regulatory strategy for encouraging long-term investment and grid modernization on the parts of both the utility and the customer. CUB believes that without a clear perspective on how the Act's interdependent requirements will work together, the Commission will not be able to motivate the utility to excel (i.e., operate efficiently).

2. AIC Position

According to AIC, CUB, through Mr. Thomas, proposes various measures to, in AIC's view, amend the terms of the Act. AIC argues that CUB's real concern appears to be not so much with the terms of AIC's MAP-P tariff, as with the new law that authorized the filing of that tariff. AIC states that CUB complains that the formula rate law creates a risk of utility over-spending, overburdens the Commission with multiple reconciliation proceedings, and recommends the Commission establish additional procedures that condition cost recovery on a utility's achievement of the Act's objective. CUB recommends the Commission establish additional requirements for AIC's formula rate filings: (1) require each cost proposal to state all costs, and the expected benefits, and require the utility to commit to achieving those benefits; (2) approve expenditure levels based on the costs of the best available performer; (3) approve a project as prudent only after gaining the necessary time perspective; (4) use long-term planning to require AIC to connect proposed expenditures to projects that promise benefits, to avoid piecemeal approval of major, long-term capital investment; and (5) establish ongoing monitoring outside of the reconciliation procedures authorized by the Act.

AIC's view is that CUB is proposing to solve a problem that does not exist. AIC says the Commission retains its substantial authority to determine the prudence and reasonableness of expenditures under Section 16-108.5 of the Act. AIC believes it is neither necessary nor appropriate to create new regulatory infrastructure and protocols to ensure that the Commission can and will exercise its authority. AIC also believes it would not be appropriate for the Commission to establish protocols that in any way frustrate the intent of the General Assembly to spur investment that improves reliability and service and creates jobs. AIC claims that imposing any requirements on such investment beyond those provided for in the Act would run counter to the General Assembly's express intent to encourage such investment.

AIC contends that the Act does not create a risk that AIC will over-spend. AIC says a utility still bears the burden of demonstrating that its costs are prudent and reasonable. AIC also says the Commission will not be rubber-stamping AIC's expenditures. According to AIC, CUB is essentially telling the Commission that the risk is that the Commission will not do its job, so the Commission has to establish protocols to keep itself in line. CUB complains that the Commission will grant piecemeal approvals without having clear visibility for an entire investment. AIC says it does not take such dim view of the Commission's vision and ability. AIC says it expects the Commission to understand and appreciate the nature and effect of the projects that will be undertaken and AIC says it is providing substantial information regarding these projects. AIC maintains that CUB's problem seems to be with the way that the legislature has decreed that the investment should proceed.

AIC contends that it is complying and will continue to comply with all of the statutory procedures regarding the making of investment and improvement of reliability and service. AIC says there are substantial penalties and other consequences if it does not so comply. AIC recommends that what it views as CUB's effort to alter the General Assembly's roadmap in this regard be rejected.

3. Commission Conclusion

CUB recommends that the Commission do the following as it implements Public Acts 97-0616 and 97-0646:

- Require each cost proposal to state all costs, and the expected benefits, and require the utility to commit to achieving those benefits.
- Approve expenditure levels based on the costs of the best available performer, which is not necessarily AIC.
- Approve a project as "prudent" only after gaining the necessary time perspective.
- Using long-term planning, require AIC to connect proposed expenditures to projects that promise benefits, to avoid piecemeal approval of major, long-term capital investments.
- Establish ongoing monitoring – not merely annual, post-hoc reviews— to ensure that project decisions can change as facts change.

AIC believes CUB's proposal is unnecessary and inconsistent with the Act. While the Commission appreciates the concerns expressed by CUB, its proposal is somewhat vague. Given the record in this proceeding, the Commission is disinclined to adopt CUB's recommendation. The Commission believes, however, that it is possible some of the concerns raised by CUB might be addressed in the rulemaking which the Commission concluded should be undertaken in Docket No. 11-0721.

XII. FINDINGS AND ORDERING PARGRAPHS

The Commission, having given due consideration to the entire record herein and being fully advised in the premises, is of the opinion and finds that:

(1) AIC is an Illinois corporation engaged in the distribution and sale of electricity and natural gas to the public in Illinois, and is a public utility as defined in Section 3-105 of the Act;

(2) the Commission has jurisdiction over the parties hereto and the subject matter herein;

(3) the recitals of fact and conclusions of law reached in the prefatory portion of this Order are supported by the evidence of record, and are hereby adopted as findings of fact and conclusions of law; the Appendix attached hereto provides supporting calculations for the rates approved herein;

(4) AIC's proposed Rate MAP-P should be approved, subject to the conclusions contained herein;

(5) the rates herein found to be consistent with Public Acts 97-0616 and 97-0646 are based on AIC's FERC Form 1 for 2010;

(6) for purposes of this proceeding, the net original cost rate base for AIC's electric delivery service operations is $2,001,788,000;

(7) the rate of return which AIC should be allowed to earn on its net original cost rate base is 8.86%; this rate of return incorporates a return on common equity of 10.05%, on long-term debt of 7.44%, on short term debt of 0.00%, and on preferred stock of 5.00%;

(8) the rate of return set forth in Finding (7) results in base rate electric delivery service operating revenues of $810,617,000 and net annual operating income of $177,358,000;

(9) AIC's electric delivery service rates which are presently in effect are inappropriate and generate operating income in excess of the amount necessary to permit the company the opportunity to earn a fair and reasonable return on net original cost rate base consistent with Public Acts 97-0616 and 97-0646; these rates should be permanently canceled and annulled;

(10) the specific rates proposed by AIC in its initial filing do not reflect various determinations made in this Order regarding revenue requirement;

(11) AIC should be authorized to place into effect Rate MAP-P, consistent with the findings of this Order, as well as the revised tariffs attached to the Appendix to AIC's Petition and reflected in AIC Ex. 9.4;

(12) AIC should be authorized to place into effect the Rate MAP-P tariff informational sheets designed to produce annual base rate electric delivery service revenues of $810,617,000, which represents a decrease of $48,088,000 or 5.60%; such revenues, in addition to other tariffed revenues, will provide AIC with an opportunity to earn the rate of return set forth in Finding (7) above; based on the record in this proceeding, this return is consistent with Public Acts 97-0616 and 97-0646;

(13) determinations regarding cost of service, rate design, and tariff terms and conditions, as are contained in the prefatory portion of this Order, are reasonable for purposes of this proceeding and consistent with Public Acts 97-0616 and 97-0646; the tariffs filed by AIC should incorporate the rates and terms set forth and referred to herein;

(14) the new tariff sheets authorized to be filed by this Order shall reflect an effective date not less than five nor more than ten working days after the date of filing, with the tariff sheets to be corrected within that time period if necessary, except as is otherwise required by Section 9-201(b) of the Act as amended;

(15) the Commission, based on AIC’s proposed original cost of plant in service as of December 31, 2010, before adjustments, of $4,920,009,000, and reflecting the Commission’s determination adjusting that figure, unconditionally approves $4,908,210,000 as the composite original cost of jurisdictional distribution services plant in service as of December 31, 2010; and

(16) all motions, petitions, objections, and other matters in this proceeding which remain unresolved should be disposed of consistent with the conclusions herein.

IT IS THEREFORE ORDERED by the Illinois Commerce Commission that the tariff sheets at issue and presently in effect for electric delivery service rendered by Ameren Illinois Company d/b/a Ameren Illinois are hereby permanently canceled and annulled effective at such time as the new electric delivery service tariff sheets approved herein become effective by virtue of this Order.

IT IS FURTHER ORDERED that Ameren Illinois Company d/b/a Ameren Illinois is authorized to file new tariff sheets with supporting workpapers in accordance with Findings (11) and (12) of this Order, applicable to electric delivery service furnished on and after the effective date of said tariff sheets.

IT IS FURTHER ORDERED that Ameren Illinois Company shall revise its formula rate template in accordance with this Order.

IT IS FURTHER ORDERED that all motions, petitions, objections, and other matters in this proceeding which remain unresolved are disposed of consistent with the conclusions herein.

IT IS FURTHER ORDERED that subject to the provisions of Section 10-113 of the Act and 83 Ill. Adm. Code 200.880, this Order is final; it is not subject to the Administrative Review Law.

By order of the Commission this 19th day of September, 2012.

(SIGNED) DOUGLAS P. SCOTT

Chairman