

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Central Illinois Public Service	:	
Company	:	
	:	98-0545
Proposed general increase in gas	:	
rates.	:	

ORDER

DATED: February 18, 1999

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: **98-0545**
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By the Commission:

I. PROCEDURAL HISTORY

On June 30, 1998, Central Illinois Public Service Company, now doing business as AmerenCIPS ("AmerenCIPS" or the "Company"), filed with the Illinois Commerce Commission ("Commission") new tariff sheets identified as Ill. C.C. No. 10F, 32nd Rev. Sheet No. 1, 7th, Rev. Sheet No. 2, 18th Rev. Sheet No. 3, 5th Rev. Sheet No. 3.1, 2nd Rev. Sheet No. 3.2, 37th Rev. Sheet No. 4, 34th Rev. Sheet No. 5, 37th Rev. Sheet No. 7, 38th Rev. Sheet No. 8, 2nd Rev. Sheet No. 8.5, 2nd Rev. Sheet No. 8.6, 3rd Rev. Sheet No. 8.7, 15th Rev. Sheet No. 10, 4th Rev. Sheet No. 10.1, 8th Rev. Sheet No. 10.2, 19th Rev. Sheet No. 10.3, 4th Rev. Sheet No. 10.4, 1st Rev. Sheet No. 10.5, 1st Rev. Sheet No. 10.6, 2nd Rev. Sheet No. 10.9, 1st Rev. Sheet No. 10.10, 5th Rev. Sheet No. 12, 5th Rev. Sheet No. 13, 1st Rev. Sheet No. 13.1, 3rd Rev. Sheet No. 14.2, 4th Rev. Sheet No. 14.3, 6th Rev. Sheet No. 15.2, 2nd Rev. Sheet No. 15.3, 8th Rev. Sheet No. 15.5, 2nd Rev. Sheet No. 15.6, 2nd Rev. Sheet No. 15.7, 9th Rev. Sheet No. 17, 4th Rev. Sheet No. 17.1, 2nd Rev. Sheet No. 17.2, 3rd Rev. Sheet No. 17.3, 3rd Rev. Sheet No. 17.4, 2nd Rev. Sheet No. 17.5, 1st Rev. Sheet No. 19, Original Sheet No. 20, Original Sheet No. 20.01, Original Sheet No. 21, Original Sheet No. 21.01, Original Sheet No. 21.02, and Original Sheet No. 21.03, hereinafter referred to as "Proposed Tariffs." The Proposed Tariffs proposed a general increase in gas rates and certain changes in the rate design, to be effective August 14, 1998.

In accordance with the requirements of Section 9-201(a) of the Public Utilities Act ("Act") (220 ILCS 5/9-201(a)) and 83 Ill. Adm. Code 255, notices of the filing of the Proposed Tariffs were timely published twice in newspapers of general circulation throughout AmerenCIPS' gas service territory. The first notice was published within ten days of the Company's filing. The second notice was published within one week of the initial notice. A copy of the proposed tariffs and a letter of transmittal were also posted in each of the Company's offices.

On July 22, 1998, the Commission suspended the Proposed Tariffs to and including November 26, 1998. On November 18, 1998, the Commission resuspended the Proposed Tariffs to and including May 26, 1999.

Petitions to intervene were filed by Archer-Daniels-Midland Company ("ADM") and the City of Carbondale, Illinois ("Carbondale"). These petitions to intervene were granted by the Hearing Examiners.

Pursuant to due notice, a prehearing conference was held on August 19, 1998 before duly authorized Hearing Examiners of the Commission at its offices in Springfield, Illinois. Thereafter, a hearing was held on December 17, 1998. Appearances were entered by counsel on behalf of the Company and Commission Staff ("Staff"). At the hearing, testimony and exhibits were submitted by witnesses for the Company and Staff. At the conclusion of the hearing on December 17, 1998, the record was marked "Heard and Taken."

The Company submitted a draft order which had previously been reviewed by Staff.

The Hearing Examiners' Proposed Order was served on the parties. Staff filed a brief on exceptions which contained minor corrections to the proposed order. No replies were filed. Staff's corrections are reflected in this order.

II. THE COMPANY'S GAS OPERATIONS

AmerenCIPS is a combination gas and electric utility. AmerenCIPS serves approximately 170,000 natural gas customers in 267 communities throughout central and southern Illinois. The Company maintains about 4,800 miles of gas mains. AmerenCIPS' gas system is interconnected to six interstate pipelines: Panhandle Eastern Pipeline Company, Trunkline Gas Company, Texas Eastern Transmission Corporation, Natural Gas Pipeline Company of America, Texas Gas Transmission Corporation and Midwestern Gas Transmission Corporation, and two other Illinois gas utilities: Northern Illinois Gas Company and Central Illinois Light Company. AmerenCIPS purchases over 99% of its gas supply from producers, gatherers and marketers and transports the gas on the six interstate pipelines. AmerenCIPS has four active on-system storage fields: Ashmore, Sciota, Johnston City and Belle Gent. The Company also operates a propane-air facility at Quincy. AmerenCIPS' peak day firm gas load is approximately 300,000 MCF and the annual throughput of the system is about 36 BCF.

III. THE PROPOSED RATE INCREASE

The Company's filing proposed an increase in base rates of approximately \$15.3 million, which would represent an increase in total revenues, exclusive of add-on taxes, of 11.14%.

The Company explained that it last increased its gas rates in March, 1992 as a result of the Commission's order in Docket No. 91-0193. The Company indicated that it has felt the effects of inflation since that time and has invested about \$75 million in gas system upgrades, improvements, new gas services and additional storage facilities. The Company explained that the combined effects of inflation and the increase in net investment caused the Company's overall rate of return on its gas business to fall to just 5.04% in 1997, well below the 9.88% approved in Docket No. 91-0193.

In its direct testimony, Staff calculated that the Company's base rates should be increased by \$6,263,000, which would represent an increase in total revenues of about 4.54%. As discussed hereafter, the Company accepted many of Staff's adjustments, and reflected certain others on a modified basis. As a result, the Company's rate proposal before the Commission is an increase in base rates of \$7.85 million, which would represent an increase in total revenues of 5.69%, or slightly more than half of the Company's initial proposal.

IV. THE EFFECT OF THE MERGER ON THE COMPANY'S BASE RATES

In Docket No. 95-0551, the Commission approved the merger whereby AmerenCIPS and Union Electric Company, now doing business as AmerenUE ("AmerenUE") became wholly-owned subsidiaries of a common holding company, Ameren Corporation ("Ameren"). As a condition of the merger approval, the Commission required, *inter alia*, that AmerenCIPS file a gas rate case within six months of the consummation of the merger. (September 10, 1997 Order in Docket No. 95-0551, p. 31) The merger closed on December 31, 1997, meaning that AmerenCIPS had to file this case before July 1, 1998. AmerenCIPS complied with this condition.

In the merger case, AmerenCIPS and AmerenUE proposed a merger savings sharing plan, pursuant to which AmerenCIPS and AmerenUE would recover -- from the total merger savings -- the merger premium paid in connection with the merger, the costs associated with completing the merger transactions, and the transition costs associated with the integration of the two company's operations. AmerenCIPS and AmerenUE also sought to retain one-half of the net savings.

The Commission declined to consider the plan in that proceeding. In its Order, the Commission stated that:

The ratemaking treatment of merger costs (including the merger premium) and savings to be adopted in a future rate case or alternative regulatory plan proceeding should be fair to both stockholders and ratepayers. The appropriate distribution of net merger savings between shareholders and rate payers will be determined in that future case.

Id. at 30. The Commission also made clear what evidence it expected from the merger applicants with respect to merger savings:

The Commission believes that [AmerenUE] and [AmerenCIPS] should present in the required rate case or alternative regulatory plan as much evidence of actual merger savings as possible [I]n an area such as labor savings, some tracking of actual savings is possible. By the time that the rate case or alternative regulatory plan is filed, [AmerenUE] and [AmerenCIPS] would know, for example, the reduction in the number of their employees that has already occurred.

Id. at 31.

In its initial filing in this case, the Company included a proposal reflecting both the costs and savings associated with the merger. The Company reflected a normalized level of estimated merger savings, which it indicated would be updated as additional information regarding workforce reductions became available. The Company proposed that it be allowed recovery of the merger premium associated with the merger, as well as all of its out-of-pocket merger transaction and transition costs. In addition, the Company proposed that it be allowed to share the net merger savings with ratepayers on a 50/50 basis.

Staff opposed the Company's proposal to recover costs associated with the merger and to share in net merger savings. The Staff indicated that neither the merger premium nor the transaction or transition costs were costs of a type whose recovery from ratepayers was appropriate. The Staff further indicated that it is not appropriate to share net cost savings within the context of a traditional rate of return proceeding. (Staff Exs. 2 and 5). Staff also proposed that rates reflect the full effect of workforce reductions and all non-labor merger savings occurring within one year of the filing of the case, in accordance with 83 Ill. Adm. Code 285.150(a). Thus, pursuant to Staff's proposal, ratepayers would receive all merger savings and the Company would bear all merger costs. Staff's merger-related adjustments reduce test year operating expenses by \$1,220,000. (Staff Ex. 2, Sch. 5)

The Company elected not to challenge Staff's position, and agreed to remove the Company's cost recovery and sharing proposals from the calculation of revenue requirement. (Ex. GSW-CIPS-3, pp. 2, 8-9). The Company also provided updated information regarding work-force levels, as it had promised to do and as Staff had proposed it be required to do. As discussed below, the changes in labor expense are fully reflected in the revenue requirement approved in this Order.

Accordingly, the record indicates that the revenue requirement in this case fully reflects all merger-related savings associated with the test year cost of service items that are recovered through base rates. (Ex. GSW-CIPS-3, pp. 8-9). Any savings associated with purchased gas costs are reflected automatically in purchased gas adjustment ("PGA") clause charges and do not require any additional Commission action to reflect them in rates charged to ratepayers. Id. at 9. As noted above, the Company has decided to withdraw its proposal for recovery of any merger costs from ratepayers. Based on the

record, the Commission finds that the Company has complied with the Commission's requirement pertaining to the provision of evidence regarding merger savings.

V. TEST YEAR

The Company's filing used an historical test year ended December 31, 1997, adjusted for all known and measurable changes occurring through June 30, 1999, as required by 83 Ill. Adm. Code 285.150(a). The Commission finds that this test year is consistent with the provisions of Part 285, and is appropriate for purposes of this proceeding.

VI. RATE BASE

In its initial filing, the Company proposed the following rate base that is based on balances and costs for the 12 months ending December 31, 1997, with certain pro forma adjustments:

	(000s)
Original Cost of Property Devoted to Gas Operations	\$257,740
Reserves for Depreciation	<u>(105,016)</u>
Net Original Cost of Property Devoted to Gas Operations	152,724
Materials and Supplies	11,754
Average Prepayments	152
Deferred Information System Development Costs	1,261
Customer Deposits	(452)
Customer Advances for Construction	(580)
Pre-1971 Investment Tax Credit	(97)
Accumulated Deferred Taxes on Income	
- Accelerated Depreciation	(17,971)
- Other	<u>(3,930)</u>
Total Original Cost Rate Base	<u>\$142,861</u>

Staff proposed certain adjustments to the rate base proposed by the Company in its initial filing. (Staff Ex. 1, Sch. 3 and 4). On rebuttal, the Company accepted the Staff's adjustments to working capital, which reduced rate base by \$152,000 (Staff Ex. 3, Sch. 6), and future use plant, which reduced rate base by \$91,000 (Staff Ex. 3, Sch. 7). The Company also reversed the Staff's adjustment to the Ashmore storage field (Staff Ex. 3, Sch. 2), which was based on an incomplete data request response. (Ex. GSW-CIPS-3, pp. 6-7) Additionally, in response to an inquiry by Staff, the Company proposed an

adjustment to reflect capitalization of meters (Ex. GSW-CIPS-3, p. 5), which increased rate base by \$218,000 (with a corresponding reduction in operating expenses), and the Company accepted the Staff's adjustments to materials and supplies ("M&S") and the Springfield office building on a modified basis. Specifically, the Company reduced its M&S balance by \$244,000 (Ex. GSW-CIPS-3, p. 6) and made a net reduction in rate base of \$407,000 in connection with the Springfield office building. (Ex. GSW-CIPS-3, pp. 7-8) The Company's revised calculation of rate base is as follows:

	(000s)
Plant in Service	\$257,222
Depreciation Reserve	<u>(104,782)</u>
Net Plant	152,440
Additions to Rate Base:	
General Materials and Supplies	495
Gas Stored Underground and Propane	11,015
Deferred Information System	1,261
Deductions from Rate Base:	
Customer Deposits	(452)
Customer Advances	(580)
Pre-1971 ITC	(97)
Accumulated Deferred Income Tax	<u>(21,901)</u>
Rate Base	\$142,181

The Commission concludes that evidence supports the use of this rate base for the purpose of developing rates in this proceeding.

VII. OPERATING REVENUES AND EXPENSES

In its initial filing, the Company proposed the following statement of operating income:

	(000s)
Operating Expenses:	
Production	\$ 2,656
Transmission	1,786
Distribution	11,016
Customer Accounts	2,538
Customer Service	585

Sales	96
Administrative and General	<u>12,976</u>
Total Operating Expenses	31,653
Depreciation and Amortization	7,695
Taxes Other than Income Taxes	2,888
Income Taxes-Based on Claimed Rate of Return	
Federal	5,399
State - Illinois	1,318
Deferred Income Taxes	<u>1,120</u>
Total Income Taxes	7,837
Return @ 9.841%	<u>14,059</u>
Total Revenue Requirements	64,132
Operating Revenue (Pro Forma)	<u>48,766</u>
Revenue Deficiency	<u>\$15,366</u>

Staff proposed several adjustments to the presentation of operating revenues and expenses reflected in the Company's initial filing. The Company elected not to challenge the Staff's adjustments to merger cost recovery (\$1,220,000) (Staff Ex. 2, Sch. 5); coal tar expenses (\$607,000) (Staff Ex. 1, Sch. 8); building rent (\$1,040,000) (Staff Ex. 1, Sch. 10); non-labor operating expenses (\$614,000) (Staff Ex. 2, Sch. 6); non-recurring payroll (\$59,000) (Staff Ex. 3, Sch. 4); rate case expense amortization (\$53,000) (Staff Ex. 3, Sch. 5); executive and director benefits (\$64,000) (Staff Ex. 4, Sch. 3); weather normalization (\$61,000) (Staff Ex. 6, Sch. 1) and advertising expense (\$23,000) (Staff Ex. 10, Sch. 2). The Company accepted Staff's method of interest synchronization. (Staff Ex. 1, Sch. 6) The Commission concludes that these adjustments are reasonable and should be accepted.

In its rebuttal testimony, in response to Staff adjustments, the Company developed revised levels of payroll, payroll taxes, pension and benefits, outside services costs and uncollectible expense. These items are discussed below. Additionally, because of changes to the rate base, the Company computed an adjustment for interest synchronization using Staff's method.

A. Payroll and Outside Services

In Docket No. 95-0551, AmerenCIPS and AmerenUE projected significant savings from a reduced work force as a result of the merger. According to projections, the merged companies would rely heavily on a service company that was to be formed in order to avoid duplication of functions.

From the time that the merger was announced until the merger was consummated, AmerenCIPS' work force steadily decreased. Because the companies were not yet merged, however, AmerenCIPS could not rely on the service company to perform the functions that had been performed by the departed employees. Accordingly, during the test year, AmerenCIPS relied on employees "borrowed" from AmerenUE pursuant to a shared-employee plan. Additionally, during the test year, AmerenCIPS relied on outside service providers to perform many functions, principally related to information technology ("IT"). Some of the IT functions related to the merger; others did not. Moreover, several IT functions were ongoing while others were non-recurring.

Subsequent to the consummation of the merger on December 31, 1997, Ameren Services Company began to perform functions for AmerenCIPS and AmerenUE, and Ameren Corporation (AmerenCIPS' and AmerenUE's parent) began to implement post-merger work force reduction efforts. The principal effort was a targeted separation program, under which employees were offered inducements to leave by October 1, 1998. At the time that this case was filed (June 30, 1998), it could not be known how many employees would elect to leave. Accordingly, in its initial filing in this proceeding, the Company indicated that the level of payroll expense (and related items, such as payroll taxes and pensions and benefits expense) would have to be adjusted to reflect post-merger labor reductions when more information was available regarding those reductions. The Company's test year labor expense included a wage rate increase.

The Company's initial filing reflected payroll expense of \$12,343,000 (including a wage rate adjustment), plus loaned employee costs of approximately \$305,000, plus outside service costs of approximately \$375,000, for total expense of \$13,023,000.

In their direct testimony, Staff witness Smith developed an adjustment to reflect information then available regarding work force levels, and Staff witness Mroczek developed a corresponding adjustment to the pro forma wage rate increase. Also, Staff witness Voss developed an adjustment to remove from the test year \$679,000 of outside service charges. These outside service charges included the costs associated with both loaned Union Electric employees and costs associated with outside service providers performing IT functions.

After the time of the Staff filing, information became available that allowed the Company to develop June 30, 1999 pro forma calculations of all components of work force costs, including direct payroll costs, service charges and outside service provider charges. The Company developed the pro forma level of expense by annualizing the labor and

service company charge data for September, 1998 (which already reflected wage rate changes), and subtracting the effect of 261 employees who departed October 1, 1998 under the targeted separation program. In the pro forma level of expense, there are no costs associated with loaned employees, and the Company included just \$125,000 of outside service charges (as compared to almost \$375,000 of outside service charges in the test year). These outside service charges are associated with ongoing IT activities, such as the Company's Y2K program and customer service and billing software matters.

For comparison purposes, the total level of pro forma payroll and outside services expense is \$12,678,000, or \$345,000 (3%) less than the 1997 historical level. This is consistent with the projections submitted in Docket 95-0551, where Ameren projected work force reductions of approximately 3%. Staff accepted the Company's proposed pro forma level of payroll and outside services expenses. The Commission concludes that this amount is reasonable and should be approved.

B. Uncollectible Expense

In its initial filing, the Company proposed uncollectible expense of \$627,000 based on the test year level of expense. In its filing, the Staff developed a three-year average of uncollectible expense, using data from the period 1995-97, totaling \$401,000. The Company indicated that since October, 1997, when employees loaned by Union Electric Company assumed control of AmerenCIPS' credit and collection and accounting functions, significant and appropriate changes have occurred with respect to uncollectible expense. AmerenCIPS has implemented a stricter collection policy and a different (and more appropriate) allocator is now used to allocate uncollectible expense associated with combined electric and gas accounts. Previously, AmerenCIPS had used a composite allocator. Now, AmerenCIPS uses an allocator based solely on revenues, because uncollectible expense is a revenue driven item.

AmerenCIPS indicated that, while the test year level of uncollectible expenses is higher than that reflected on AmerenCIPS' books in prior years, it is reasonable and properly reflects the level of expense that the Company will incur when the new base rates go into effect. The Company stated that the allocator being used for combined accounts is appropriate, and uncollectible expense for just the first 9 months of 1998 exceeded the test year level. Further, budgeted 1999 expense exceeds the 1998 level.

AmerenCIPS is willing, however, to phase in the effect of the changes in the collection policy and the allocation of uncollectible expense between electric and gas. The Company has developed an average uncollectible expense for the period 1995 through September, 1998 of \$551,000, which results in an uncollectible percentage of .3635% of total revenues. The use of this percentage produces a test year expense level of \$578,000 based on the rebuttal revenue requirement.

Staff agreed that the Company's revised calculations of uncollectible expense is reasonable for use in this proceeding. The Commission concludes that the Company's revised calculation of uncollectible expense is reasonable and should be approved.

C. Approved Operating Income Statement

Giving effect to the adjustments to operating revenues and expenses approved hereinabove, and the rate of return on original cost rate base of 8.51% hereafter allowed in this Order, the Commission concludes that for purposes of this proceeding, the Company's Operating Income Statement for the Test Year ended December 31, 1997, at approved rates, is as follows:

	(000s)
Operating Revenue	\$ 56,677
Uncollectible Accounts	578
Production	2,049
Transmission	1,786
Distribution	10,792
Customer Accounts	1,911
Customer Service	585
Sales	96
General and Administrative	9,740
Depreciation and Amortization	7,682
Taxes Other Than Income	<u>2,963</u>
Total Operating Expense Before Income Taxes	38,182
State Income Tax	970
Federal Income Tax	4,305
Deferred Taxes and ITC's Net	<u>1,120</u>
Total Operating Expenses	<u>44,577</u>
NET OPERATING INCOME	<u>\$ 12,100</u>

The Operating Income Statement hereinabove reflects the gas rate increase of \$7,850,000 or 5.69%, which is granted in this Order.

VIII. COST OF CAPITAL

In its initial filing, the Company proposed the use of a December 31, 1997 capital structure in setting rates that contains 46.062% long-term debt, 6.604% preferred stock and 47.334% common equity. Relying on the comparable earnings model that was

applied to two groups of comparable companies, a Local Distribution Company Group and a General Industry Group, the Company determined that its cost of common equity is 13.25%. This cost of common equity, coupled with the embedded costs of long-term debt and preferred stock, resulted in a recommended overall cost of capital (return on rate base) by the Company of 9.841%.

Staff witness Rungren adjusted the Company's proposed capital structure in two ways. First, he used the "net proceeds" amount for the preferred stock balance, rather than the "face amount outstanding" balance used by the Company. Second, he included short-term debt in the capital structure. He noted that the Company maintains a substantial short-term debt balance that is used to provide working capital and finance construction work in progress ("CWIP"). He indicated that the "CWIP Balance Accruing Allowance for Funds Used During Construction ("AFUDC")" is not available for the Company. The amount of short-term debt that he included in the capital structure is the 12-month average balance for the 12 months ending December 31, 1997. Mr. Rungren noted that the Company's short-term debt is composed entirely of commercial paper that principally has 1-day, 30-day and 60-day terms. He averaged the rates for those terms, and concluded that the Company's cost of short-term debt is 5.16%.

To determine the Company's cost of common equity, Mr. Rungren used a discounted cash flow ("DCF") model and a risk premium model. His risk premium analysis used the capital asset pricing model ("CAPM"). His DCF and risk premium analyses were performed on a sample of nine public utilities that he determined were comparable in risk to the Company. His DCF analysis produced a cost of common equity for the comparable sample in the range of 10.10% to 11.02%, while his risk premium analysis produced a cost of common equity in the range of 10.36% to 11.02%. In developing his recommended cost of equity for the Company, he considered his DCF and risk premium estimates for the comparable sample, the observable 6.96% rate of return on Aa-rated long-term utility debt, the 14.82% estimate for the market return, and the average of U.S. Treasury bill and U.S. Treasury bond yields as the proxy for the risk-free rate.

Mr. Rungren formed a cost of equity range for the sample by (1) averaging the DCF-derived estimates of the required rate of return on common equity and rounding to the nearest ten basis points, 10.60%, (2) using the average of the U.S. Treasury bill and U.S. Treasury bond yields as the risk-free rate proxy and rounding the resulting risk premium estimate to the nearest ten basis points, 10.70%, and (3) expanding the resulting range, 10.60% to 10.70%, by sixty basis points to recognize the imprecision inherent in estimates of the cost of common equity. Based on his entire analysis, Mr. Rungren concluded that a reasonable cost of common equity for the Company's gas operations ranges from 10.30% to 11.00%, with a midpoint estimate of 10.65%.

Mr. Rungren concluded that the Company's overall cost of capital is 8.51%. This overall cost of capital was developed as follows:

<u>Component</u>	<u>Ratio</u>	<u>Cost</u>	<u>Weighted Cost</u>
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Short-term debt	3.35%	5.16%	0.17%
Long-term debt	44.58	7.11	3.17
Preferred Stock	6.26	4.57	0.29
Common Equity	<u>45.81</u>	<u>10.65</u>	<u>4.88</u>
Total		100.00	8.51%

The Company subsequently agreed to Staff's determination of its overall cost of capital.

The Commission finds, based on the evidence, that it is just and reasonable to allow AmerenCIPS the opportunity to earn an overall return of 8.51% on net original cost rate base.

IX. CLASS COST OF SERVICE AND INTERCLASS REVENUE ALLOCATION

In its initial filing, the Company proposed moving each rate class to its fully embedded cost of service. In the past, the Company has moved toward such a goal, but, in the interests of gradualism, current rates reflect certain, and at times significant, interclass subsidies.

Staff witness Johnson was generally in agreement with the Company's cost of service study "(COSS)", but proposed using the average and peak ("A&P") method for allocating capacity-related transmission and distribution costs, instead of the average and excess method used by the Company. Mr. Johnson stated that the A&P allocator is a hybrid approach that allocates costs by both peak demands and average demands. The peak demand component recognizes that a transmission and distribution "(T&D)" system is sized to meet maximum annual demands. However, there is also an average demand component because meeting peak demands is not the only factor that shapes investment in a T&D system.

Mr. Johnson further noted that another factor to be considered is the economic motivation to construct a T&D system. This factor is more appropriately reflected by average demands than peak demands. Because demands throughout the year are necessary to generate sufficient revenues to justify investment in a T&D system, these year round demands are reflected in the average demand, but not the peak-demand component of the A&P allocator.

Mr. Johnson indicated that safety and reliability investments constitute another factor more appropriately reflected by average demands than by peak demands. These are concerns, not only for the peak day, but for every day of the year that gas is consumed, which the average demand component reflects.

Additionally, Mr. Johnson pointed out that the A&P allocation method has been used by Staff and accepted by the Commission in recent natural gas rate case proceedings, including the following dockets:

- Illinois Gas Company; 98-0298
- United Cities Gas Company; 96-0618
- Mt. Carmel Public Utility Company; 95-0418
- Northern Illinois Gas Company; 95-0219
- Peoples Gas Light and Coke Company; 95-0032
- North Shore Gas Company; 95-0031
- Central Illinois Light Company; 94-0040

The Company proposed allocating intangible and general plant using production, storage, T&D, customer expenses and labor only. Staff witness Johnson recommended using total natural gas plant in service, excluding intangible and general, as a proper allocation methodology for intangible and general plant. Mr. Johnson stated his belief that intangible and general plant allocations should take into account all aspects of plant in service since that is the cost these allocations support. Additionally, Staff has employed, and this Commission has accepted, this method in the last several gas rate proceedings, as noted above.

Staff witness Johnson's interclass revenue allocation ("IRA") methodology focuses on eliminating subsidies at present rates, while the Company's approach focuses on eliminating such subsidies at proposed rates. The Company did not have any objection to Staff's COSS and IRA approaches and incorporated those approaches in the development of its "rebuttal rates," i.e., its rates reflecting the revised calculation of revenue requirement submitted on rebuttal. (Ex. RJM-CIPS-2, Sch. 1)

The Commission concludes that Staff's COSS and IRA methodology are reasonable and should be used in determining rates in this proceeding.

X. RATE DESIGN

A. Overview

The Company proposed certain significant changes in the rate design and class definitions, in an effort to further unbundle the services offered by the Company, and to properly reflect the nature of the services offered by the Company. These changes were intended to simplify the terms and conditions on which customers (principally those taking transportation service) receive services from the Company.

A principal change proposed by the Company was the elimination of the current Riders C and D, which provide for Transportation of Customer-Owned Gas and Standby-Service, respectively. AmerenCIPS proposed to replace these riders with a new Rider T which incorporates the provisions of Riders C and D. Additionally, the Company proposed

a new Rider S, which provides the same service options for System Gas Service as are available under Rider T for transportation service.

Staff proposed several revisions to the Company's rate design.

B. Riders S & T

1. Facilities Charges

The Company proposed a Facilities Charge of \$55 per month for Rider T (Transport Gas and Standby Service) and Rider S (System Gas Service). Additionally, an administrative charge of \$60 per month was proposed for Rider T. Staff reviewed information provided by the Company and agreed with the charges. The Commission concludes that the charges are reasonable and should be approved.

2. Language Changes

Staff witness Johnson indicated that he did not oppose the introduction of Riders S and T. He did, however, express a concern with certain language in the Riders. Specifically, both Riders S and T, as filed, include the phrase "Service option for customers that have a somewhat constant usage of gas each month throughout the year." Mr. Johnson expressed concern that the term "somewhat constant" is ambiguous. He proposed that the Company revise this language on rebuttal. The Company proposed to replace this phrase in each Rider with the following: "Service option for high load factor customers that do not want to reduce their gas consumption during periods of curtailment." This change alleviated the concerns that Staff expressed, and should be approved.

3. Storage and Production

Staff witness Iannello testified that Riders S and T fail to provide access to storage and production resources that is proportionate to the allocation of storage and production ("S&P") costs for certain customers. He noted that, while all Rate 11 (General Delivery Service) and 20 (Large Use - Firm Delivery Service) customers are allocated S & P-related costs in their base rates, only those customers that pay additional PGA-related charges for System Gas Service (under Rider S) or Transport Gas and Stand-by Service (under Rider T) are given penalty-free access to customer-owned gas in storage or to Company-provided "system" gas and manufactured propane during periods of supply limitation. Mr. Iannello recommended modifications to the Riders that would provide greater access to S & P resources for Designated Full System Gas/Transport and Standby and Designated Partial System Gas/Transport and Standby Customers.

The Company indicated that Staff's proposal would put great strain on the Company's existing S & P resources. The Company stated that it does not have adequate S & P resources to give these customers the type of access proposed by the Staff. The Company agreed, however, that Staff's underlying point should be addressed: why are

customers without penalty-free access to S & P resources being allocated S & P costs on the same basis as those who do receive such access?

All classes rely on S & P resources to some extent, because those resources are used to back up the system as a whole. The resources also provide additional peak day benefit to specific customers. The Company acknowledged that the problem with its initial cost of service/rate design proposal was that it did not allocate costs in recognition of these facts.

The Company reexamined the allocation of S & P costs among the classes. The Company identified what uses are made of S & P resources, and then identified how each class uses them. The Company estimated that approximately 59% of S&P costs are associated with meeting peak day demand. These peak day demand-related costs were then allocated to each class based on its percentage of total system back-up.

As a result, the costs allocated to Rate 20 were reduced by \$288,000, and were reallocated to Rate 11 (\$73,000) and Rate 10 (\$215,000). The Company agreed that these reallocations reflect a more appropriate assignment of cost responsibility for S&P facilities to the rate classes. The Commission concludes that these reallocations are reasonable and should be approved.

C. Weather Normalization

The Company proposed to normalize usage for weather changes to ensure that test period sales reflect normal weather (i.e., temperature), rather than unusually warm or cold weather. For example, if test period sales were based on an extremely cold winter, sales would be overestimated compared to a normal winter, and would under-collect the revenue requirement; and, if based on a warm winter, sales would over-collect the revenue requirement. If test period sales are not weather normalized, the rates may not collect the authorized revenue requirement during a period of normal weather.

A regression analysis was performed using billing cycle sales per customer as a function of billing cycle heating degree days ("HDD"). (Ex. JRP-CIPS-1, p. 2). The resulting regression equation explains the relationship between sales per customer and HDD. As the number of HDD rises, the Company's regression equation increases sales per customer accordingly. Likewise, as the number of HDD falls, the regression equation reduces sales per customer accordingly. The regression indicated a strong direct relationship between sales per customer and HDD. A thirty three-year normal HDD was calculated using weather data from 1965-1997. Historical temperatures were obtained from Quincy, Mattoon and Marion weather stations and a weighted average was developed. (Ex. JRP-CIPS-1, p. 3).

Staff witness Johnson agreed with the Company's weather normalization methodology and adjustments to classes as a whole but had concerns with the allocation of them adjustments to individual months and the consequent impact on usage in the

residential space heating rate blocks and on resulting revenues. The Company's methodology produced significant adjustments to actual sales in the summer months even though normal HDDs were minimal for each summer month. Mr. Johnson proposed taking the total Company proposed therm reduction for the residential space heating class (i.e., 2,336,724 therms) and dividing it by the total of each month's difference in actual HDD and average HDD, which resulted in therms per HDD. The resulting therms per HDD were multiplied by each month's difference in actual HDD and average HDD to arrive at a monthly adjustment. Next, Mr. Johnson calculated the therms per customer for actual usage and normalized usage and determined which block should be adjusted, based upon whether the therms per customer were less than 50 therms or greater than 50 therms. After block adjustments were determined, Mr. Johnson calculated the revenue adjustment based upon current therm charges. (Staff Ex. 6.0, Schedule 1)

The Company agreed with Staff's adjustment. (Ex. GSW-CIPS-3, p. 3). The Commission concludes that the Company's weather normalization methodology and Staff's adjustment to the residential class should be used in determining rates in this proceeding.

D. Rate 10 - Residential

The Company proposed increasing the current \$7 monthly customer charge by \$2.50 to \$9.50. This proposed charge would recover most but not all customer costs, which exceed \$10/month, according to the Company's COSS. (Ex. RJM-CIPS-1 p. 6). The Company proposed recovering remaining costs through an increase in the delivery charges from \$0.1550 per therm to a proposed \$0.2090 per therm for the first 50 therms of gas and an increase in the second block of over 50 therms from \$0.1056 per therm to \$0.1417 per therm. (Ex. GSW-CIPS-1, Schedule E-2, p. 9).

Staff witness Johnson agreed with the Company's proposed Customer Charge of \$9.50 per month. While this customer charge will not recover all customer costs, it represents movement towards cost recovery without causing an excessive rate impact on small use residential customers. The unrecovered revenue requirement for the customer charge is then recovered in the first block rate along with the average demand rate for the class. The rate in the second block consists of the average demand rate for the class. (Staff Ex. 6.0, pp. 28-29).

The Company accepted Staff's rate design for this class. (Ex. RJM-CIP-2, p. 4). Subsequently, the parties agreed to charges consisting of a customer charge of \$9.50 per month and delivery charges of \$0.1589 per therm for the first 50 therms and \$0.1164 per therm for all remaining therms, based on the final revenue requirement figure. The Commission concludes that this rate design is reasonable and should be approved.

E. Rate 11 - General Delivery Service

The Company proposed a customer charge increase from \$16 to \$28.50. The proposed customer charge is set at the Company's cost of service. The balance of the proposed class revenue increase is recovered in a single delivery charge of \$.1631 per therm. (Ex. RJM-CIPS-1 at 13-14 and Schedule 1.2, p. 10).

Mr. Johnson proposed basing Rate 11 customer charges on meter capacity with two classes as follows: up to 250 cubic feet per hour and over 250 cubic feet per hour ("cf/hr"). Staff believes that since there is such a diverse group of customers with substantially different sized meters in the Rate 11 class, separating them by meter capacity will further eliminate intraclass subsidies. Additionally, Mr. Johnson proposed a single block delivery charge for Rate 11. (Staff Ex. 6.0, pp. 30-31).

The Company accepted Staff's rate design for this class. (Ex. RJM-CIPS-2, p. 5). Subsequently, the parties agreed to charges consisting of customer charges of \$18.00 per month for meters using less than or equal to 250 cf/hr. and \$45.00 per month for meters using greater than 250 cf/hr. and a single delivery charge of \$0.1246 per therm, based on the final revenue requirement figure. The Commission concludes that this rate design is reasonable and should be approved.

F. Rates 20 and 21 - Large Use (Firm and Interruptible)

The Company's COSS indicates that the Rate 20 class is paying more than the cost to serve them. Therefore, the Company proposed an overall rate decrease for the class. The Company proposed that the monthly customer charge be increased from \$80 to \$100 per month. (Ex. RJM-CIPS-1 at 14). However, at the Company's initially proposed levels, the customer charge was not fully cost-based. The Company proposed that the single delivery charge be decreased from \$0.0753 per therm to \$0.0541 per therm. (Ex. RJM-CIPS-1, Schedule 1.2, p. 11).

Mr. Johnson disagreed with the Company's proposal to increase the customer charge such a limited amount when the COSS suggested a substantial increase. Both the Company's and Staff's COSS calculated customer costs that were much higher. Mr. Johnson suggested that customers under Large-Use service should face rate elements that are set to recover their respective allocated cost (i.e., customer, demand and/or commodity) to the extent possible. Mr. Johnson therefore proposed a customer charge that was fully cost-based for the class, i.e., \$348 per month. Additionally, Mr. Johnson proposed a single block delivery charge for Rate 20. (Staff Ex. 6.0, pp. 33-36 and Schedule 6, p. 3).

The Company proposed modifying the eligibility requirements for Rate 21. The rate would only be applicable to those customers that are being served in areas of the gas delivery system that are inadequate to provide firm delivery service during the peak season. This proposal will shift 141 current interruptible customers to Rate 20 (Firm Delivery Service). Because of the provision change and shifting of customers, the Company found it necessary to combine all large use delivery customers (i.e., firm and

interruptible) into a single class for cost of service modeling. (Ex. RJM-CIPS-1, pp. 14-17). The proposed customer charge would be set at the Rate 20 level, a decrease from \$136 to \$100 per month. A single delivery charge of \$0.0406 per therm was determined by discounting the Rate 20 distribution charge by 25%. Company witness Mill stated that the discount is reflective of the proportion of the year represented by the peak season period during which the delivery requirements of interruptible customers were likely to be curtailed. Id.

Mr. Johnson agreed that the rate should be limited to those customers who are actually subject to being interrupted. Mr. Johnson also found it necessary to combine Rates 20 and 21 for cost of service purposes. The Company pointed out that the few remaining interruptible customers (13) lack specific information that is necessary to properly allocate costs to the customers. Additionally, the Company has not kept the level of detail needed to perform a cost-of-service study for such a small segment of an existing class. (Staff Ex. 6.0, pp. 37-38).

Mr. Johnson agreed that the Rate 21 customer charge should be set at the Rate 20 level, which should be fully cost-based. Mr. Johnson stated that the correct way to determine the delivery charge would be to base it on demand related costs derived from the COSS. However, the interruptible class could not be separated for cost of service purposes. Therefore, some type of method has to be used to derive a delivery charge. While there may be various ways to determine the delivery charge for Rate 21 customers, all of which probably would not be cost-based under the circumstances, Mr. Johnson indicated that use of the Company's proposed 25% discount method is reasonable until a more precise class cost of service can be determined in a future proceeding.

The Company agreed in principle with the concept of moving to fully cost-based customer charges. However, it was necessary to combine all large use delivery service customers into a single class for cost of service modeling. The Company indicated that the substantial movement toward fully cost-based rates, as proposed by the Staff in this case, would cause extensive rate migration that would be difficult to reflect in the COSS and rate design. There is a point at which smaller customers would find it beneficial to migrate to Rate 11 because their overall cost would be lower. The Company does not have sufficient data, however, to predict precisely the level of migration and to adjust class revenue requirements and rates accordingly. The rate migration would then produce a significant risk of under- or over-recovery of the revenue requirement.

The Company reviewed the available data and determined that an increase in the customer charge to \$150/mo. would not create extraordinary rate migration and would also offer the advantage of a more gradual change in the customer charge for existing customers. Accordingly, the Company proposed that the customer charges for Rates 20 and 21 be increased to \$150/mo. and that the classes be adjusted to reflect the minimal migration that is anticipated. The Company's rebuttal rates reflected these changes.

Since Rates 20 and 21 currently have a one block delivery charge and the proposed delivery charges are lower than the current delivery charges, the Company proposed that the single block structure be maintained and the unrecovered customer costs be recovered through a single block delivery charge. While unrecovered customer costs are often recovered in the first block along with the average demand rate for the class and all other costs recovered in the last block, maintaining Rates 20 and 21 with one block will ensure continuity while not imposing unnecessary impacts on these classes. Additionally, the Company does not maintain adequate data on which to determine multiple delivery charge blocks for the newly-defined Rates 20 and 21. Consequently, establishing delivery charge blocks with inadequate data would produce a significant risk of under- or over-recovery of the revenue requirement ultimately approved in this proceeding. Under the Company's proposal, there would be a definite movement toward cost-based rates while keeping the current rate structure in place.

Staff agreed with the Company's proposals for Rates 20 and 21. The customer charge for Rates 20 and 21 is \$150 per month and the delivery charges are \$0.0547 for Rate 20 and \$0.0409 for Rate 21, based on the final revenue requirement figure. The Commission concludes that these charges are reasonable and should be approved.

G. Rate 23-Special Contract Service

In the Commission order approving Rate 23, the Commission stated that:

Should CIPS file a rate case during the period in which contracts under this rate are in effect, the Commission intends that other customers not be responsible for any shortfall between the cost of serving a Rate 23 customer and the revenues generated under that customer's contract.

Order in Docket No. 93-0235, p. 2

According to the Company's and Staff's COSS, Rate 23 customers have an above system rate of return at both present and proposed rates. Therefore, other customers are not subsidizing this class on an embedded basis. Additionally, this class is exempt from any rate increase/decrease resulting from this rate case and therefore was not included in Staff's IRA proposal. (Staff Ex. 6.0, pp. 43-44).

G. Miscellaneous Rates/Fees

The Company proposed increasing the dishonored check charge from \$10 to \$15. (Ex. JRC-CIPS-1, p. 3). The Company indicated that the cost to process checks has increased since this charge was last approved by the Commission. Additionally, the proposed charge is in line with other Illinois utilities. Staff witness Johnson reviewed information provided by the Company and does not oppose the Company's proposal as this increase recovers the associated costs.(Staff Ex. 6.0, p. 42). The Commission concludes that the Company's proposed increase is reasonable and should be approved.

The Company proposed using the same amount of revenue from late payment fees at proposed rates as collected in the test year at present revenues. Mr. Johnson disagreed with the Company's proposal. Mr. Johnson stated that late payment fees are a percentage of the unpaid balance of a customer's bill. If the Company receives an increase in rates, the amount of the bills (all else being equal) will increase, thereby creating additional revenues for the Company when the customer pays after the due date. Mr. Johnson proposed that late payment fee revenues be increased based on the same percentage that total revenues increase, excluding other revenues. The Company accepted Staff's proposal. (Ex. RJM-CIPS-2, p. 6). The Commission concludes that Staff's proposal is reasonable and should be approved.

Staff witness Maple proposed that the Company update tariff sheet 10.3 to change references to General Order 172 to 83 Ill. Adm. Code 280. (Staff Ex. 9.0, p. 3) The Company indicated that it will do so in its compliance filing in this case. (Ex. RJM-CIPS-2, p. 6)

Mr. Maple also proposed that the Company define the term "regular working hours" as it appears on tariff sheet no. 10.3. (Staff Ex. 9.0, p. 4) The Company thereafter proposed to define "regular working hours" as "8:00 A.M. to 5:00 P.M. Monday through Friday." (Ex. RJM-CIPS-2, p. 6) The Commission concludes that this definition is reasonable and should be approved.

Mr. Maple further proposed that the Company revise its reconnection fee charges to correct an error in the Company's calculations that was discovered after this case was filed. (Staff Ex. 9.0, pp. 6-7) The Company agreed to do so, and proposed reconnection fees of \$55.00 per connection point during regular working hours and \$100.00 per connection point outside of regular working hours. (Ex. RJM-CIPS-2, pp. 6-7) The Commission concludes that these reconnection fees are reasonable and should be approved.

XI. FINDINGS AND ORDERING PARAGRAPHS

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) AmerenCIPS is an Illinois corporation engaged in the distribution and sale of natural gas to the public in Illinois and is a public utility as defined in Section 3-105 of the Public Utilities Act;
- (2) the Commission has jurisdiction over the parties and the subject matter herein;
- (3) the recitals of fact and conclusions reached in the prefatory portion of this Order are supported by the evidence of record, and are hereby adopted as

findings of fact; the Appendix attached hereto provides supporting calculations for various portions of this Order;

- (4) the test year for the determination of the rates herein found to be just and reasonable should be the 12 months ending December 31, 1997, as adjusted; such test year is appropriate for purposes of this proceeding;
- (5) for purposes of this proceeding, the original cost rate base for the Company's gas operations for the test year ending December 31, 1997, as adjusted, is \$142,181,000;
- (6) a just and reasonable return which AmerenCIPS should be allowed to earn on its net original cost gas rate base is 8.51%; this rate of return incorporates a return on common equity of 10.65%;
- (7) the rates of return set forth in finding (6) result in base rate gas operating revenues of \$56,677,000 and net annual operating income of \$12,100,000 based on the test year approved herein;
- (8) AmerenCIPS' rates which are presently in effect are insufficient to generate the operating income necessary to permit AmerenCIPS the opportunity to earn a fair and reasonable return on net original cost rate base; these rates should be permanently canceled and annulled;
- (9) the specific rates proposed by AmerenCIPS in its initial filing do not reflect various determinations made in this Order regarding revenue requirement, cost of service allocations and rate design; AmerenCIPS' proposed rates should be permanently canceled and annulled consistent with the findings herein;
- (10) AmerenCIPS should be authorized to place into effect tariff sheets designed to produce annual base rate revenues of \$56,677,000, which represents an increase of \$7,850,000 or 5.69%; such revenues will provide AmerenCIPS with an opportunity to earn the rate of return set forth in finding (6) above; based on the record in this proceeding, this return is fair and reasonable for AmerenCIPS;
- (11) determinations regarding cost of service, interclass revenue allocations, rate design and tariff terms and conditions, as are contained in the prefatory portion of this Order, are reasonable for purposes of this proceeding; the tariffs filed by AmerenCIPS should incorporate the rates and rate design set forth and referred to herein;
- (12) new tariff sheets authorized to be filed by this Order should reflect an effective date not less than three (3) working days after the date of filing, with the tariff sheets to be corrected, if necessary, within that time period.

IT IS THEREFORE ORDERED by the Illinois Commerce Commission that the tariff sheets presently in effect for gas service rendered by Central Illinois Public Service Company are hereby permanently cancelled and annulled effective at such time as the new gas tariff sheets approved herein became effective by virtue of this Order.

IT IS FURTHER ORDERED the proposed tariffs seeking a general increase in gas rates, filed by Central Illinois Public Service Company on June 30, 1998, are permanently cancelled and annulled.

IT IS FURTHER ORDERED that Central Illinois Public Service Company is authorized to file new tariff sheets with supporting workpapers in accordance with Findings (10), (11) and (12) of this Order, applicable to gas service furnished on and after the effective date of said gas tariff sheets.

IT IS FURTHER ORDERED that subject to the provisions of Section 10-113 of the Public Utilities Act and 83 Ill. Admin. Code 200.800, this Order is final; it is not subject to the Administrative Review Law.

By order of the Commission this 18th day of February, 1999.

(SIGNED) RICHARD L. MATHIAS

Chairman

(S E A L)