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OPC – Exhibit 204
David Murray
Surrebuttal Testimony
File No. ER-2022-0337

Exhibit No.:	___________
Issue(s):	Rate of Return (ROR)/ Capital Structure
Witness/Type of Exhibit:	Murray/Surrebuttal
Sponsoring Party:	Public Counsel
Case No.:	ER-2022-0337

SURREBUTTAL TESTIMONY

OF

DAVID MURRAY

Submitted on Behalf of the Office of the Public Counsel

UNION ELECTRIC COMPANY D/B/A AMEREN MISSOURI

CASE NO. ER-2022-0337

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Denotes Confidential Information that has been redacted

March 13, 2023

PUBLIC

TABLE OF CONTENTS

Testimony	Page
True-Up Recommendation	2
Capital Structure	3
Increased Debt Capital from Lower Business Risk	4
Fiduciary/Conflicts of Interest	6
Other Missouri Utility Companies' Financial Risk Profiles	12
Comparison to Ameren Illinois' Capital Structure Arguments Before the Illinois Commerce Commission	13
Pro Forma Impact of Capital Structure on Credit Profile	15
Parent/Subsidiary Financing Relationship	17
Investor Expectations on Ratemaking Capital Structure	27
Four Criteria – Subsidiary vs. Parent Capital Structure	28
Ann E. Bulkley's Rebuttal Testimony	35
Return on Equity	35
Seoung Joun Won's Rebuttal Testimony	53
Summary and Conclusions	55

SURREBUTTAL/TRUE-UP DIRECT TESTIMONY

OF

DAVID MURRAY

UNION ELECTRIC COMPANY d/b/a AMEREN MISSOURI

FILE NO. ER-2022-0337

1 **Q. Please state your name and business address.**

2 A. My name is David Murray and my business address is P.O. Box 2230, Jefferson City,
3 Missouri 65102.

4 **Q. Are you the same David Murray who previously filed Direct and Rebuttal Testimony**
5 **in this case?**

6 A. Yes.

7 **Q. What it the purpose of your testimony?**

8 A. To respond to Ameren Missouri witnesses Darryl T. Sagel's and Ann E. Bulkley's rebuttal
9 testimonies as they relate to rate of return ("ROR") and capital structure. I also address the
10 rebuttal testimony of Staff witness Seoung Joun Won, PhD.

11 I will also update my ROR recommendation to consider Ameren Corp's and Ameren
12 Missouri's financial activities through the ordered true-up date in this case, December 31,
13 2022.

14 **Q. In what order will you address these issues/witnesses?**

15 A. First, I will update my ROR recommendation based on financial data through the true-up
16 date. Second, I will address capital structure, which was the sole ROR issue addressed by
17 Mr. Sagel. Dr. Won also disagrees with the premise of using Ameren Corp as a proxy for
18 a fair and reasonable ratemaking capital structure for Ameren Missouri. Finally, I will
19 address Ms. Bulkley's and Dr. Won's responses to my recommended allowed ROE of
20 9.25% for Ameren Missouri's integrated electric utility operations.

1 **TRUE-UP RECOMMENDATION**

2 **Q. Has your analysis of Ameren Corp's and Ameren Missouri's financial activities**
3 **through the true-up period caused you to change your ROR recommendation?**

4 A. Yes but only for changes in the cost of long-term debt. Ameren Missouri's cost of long-
5 term debt increased by two basis points from 3.91% to 3.93%. I included this slight
6 increase in my updated recommended ROR.

7 **Q. Did any of Ameren Corp's or Ameren Missouri's financial activities between the**
8 **update period, June 30, 2022 and the true-up period, December 31, 2022, cause you**
9 **to change your opinion as to a reasonable recommended common equity ratio?**

10 A. No. In fact, my analysis of capital flows between Ameren Corp and Ameren Missouri
11 during the fourth quarter of 2022 provided further evidence as to the appropriateness of
12 considering Ameren Corp's capital structure for purposes of setting Ameren Missouri's
13 ratemaking ROR.

14 **Q. Is your recommended ROR as of the true-up date attached as a schedule?**

15 A. Yes. The first page of Schedule DM-S-1 shows my recommended ROR as of the true-up
16 date. The remaining pages of Schedule DM-S-1 reflect the information I analyzed for
17 purposes of developing my recommended ratemaking capital structure as of the true-up
18 date.

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1 **CAPITAL STRUCTURE**

2 **Q. Summarily, what are the main points of disagreement between you and the other**
3 **witnesses over an appropriate ratemaking capital structure for Ameren Missouri's**
4 **ROR?**

5 A. The other witnesses support the use of Ameren Missouri's per books capital structure.[1]
6 They maintain this is the appropriate ratemaking capital structure because, in their view, it
7 is independently managed for its own benefit, and presumably for the benefit of Ameren
8 Missouri's ratepayers. While I agree that Ameren Missouri's capital structure is carefully
9 managed, it is managed for one primary purpose, achieving a constant 52% authorized
10 equity ratio regardless of changes in business and economic conditions. The fact that
11 Ameren Missouri's common equity ratio has been maintained, despite declining business
12 risk since 2018, while Ameren Corp's common equity ratio has consistently declined
13 during the same period, deserves close scrutiny. Despite Ameren Missouri's reduced
14 business risk due to the passage of utility-favorable legislation in Missouri, such as the
15 initial passage of legislation allowing Ameren Missouri's election of plant in service
16 accounting ("PISA") through 2023, its amendment to allow for automatic extension
17 through 2028, and the ability to securitize both undepreciated balances of fossil-fuel plants
18 retired early and extraordinary costs such as those incurred during extraordinary weather
19 events, Ameren Missouri's equity ratio hasn't budged from the 52% target over the last
20 twelve years. It would be less egregious for ratepayers to foot the bill for a 52% equity
21 ratio if Ameren Corp targeted this more conservative level for itself as well, but instead, its
22 common equity ratio has been in the 42% to 43% range.

23 I will show that Ameren Missouri's capital structure has not been managed for its own best
24 interests or for the best interests of its ratepayers. Ameren Missouri's ratepayers are paying
25 for the costs of more shareholder friendly ratemaking mechanisms, but not receiving the

[1] Mr. Sagel's and Dr. Won's preferred stock and long-term debt balances are adjusted slightly for premiums, discounts and issuance expenses to arrive at a carrying value/net proceeds balance, but their capital structure recommendations are premised on Ameren Missouri's balance sheet ratios, not Ameren Corp's balance sheet ratios.

1 benefit of the lower-cost capital structure these mechanisms allow (i.e. higher debt
2 capacity).

3 *INCREASED DEBT CAPACITY FROM LOWER BUSINESS RISK*

4 **Q. Does Mr. Sagel recognize that since Ameren Missouri was allowed to elect PISA**
5 **subsequent to the passage of Senate Bill ("SB") 564, Ameren Corp's debt capacity has**
6 **increased?**

7 A. Yes, but it is his position that this is only one factor Moody's considered when it lowered
8 Ameren Corp's funds from operations to debt ("FFO/debt")[2] downgrade threshold to 17%
9 from 19%. Mr. Sagel indicates Ameren Corp's increased debt capacity was also due to "a
10 strong track record of strategy execution within the supportive regulatory frameworks of
11 Ameren Corporation's subsidiaries, Ameren Illinois and ATXI."[3]

12 **Q. Did Moody's lower its FFO/debt downgrade threshold for Ameren Corp's other**
13 **operating subsidiaries, Ameren Illinois or ATXI?**

14 A. Not to my knowledge.

15 **Q. Is it logical for the operating subsidiaries, which directly own the assets, not to have**
16 **increased debt capacity due to supportive regulatory frameworks?**

17 A. No.

18 **Q. Then why would Moody's lower its downgrade threshold for Ameren Corp rather**
19 **than its downgrade thresholds for Ameren Missouri, Ameren Illinois, and ATXI?**

20 A. Because, as I will explain in more detail later in my testimony, the officers who represent
21 Ameren Corp, Ameren Missouri, Ameren Illinois, and ATXI when interacting with the

[2] Although there are subtle differences between Moody's CFO Pre-WC/Debt ratio and an FFO/debt ratio, I will generally refer to Moody's CFO Pre-WC/Debt ratio as "FFO/debt," which is similar to Mr. Sagel's reference to such in his rebuttal testimony.
[3] Sagel Rebuttal, p. 21, line 26 – p. 22, l. 1.

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1 rating agencies are acting as fiduciaries for Ameren Corp rather than each of Ameren
2 Corp's subsidiaries, including Ameren Missouri.

3 **Q. Mr. Sagel testifies that Moody's rejected Ameren Corp's management's argument to**
4 ** ____
5 ____
6 **[4] Is he correct?**

7 A. No. ** ____
8 ____
9 ____
10 ____
11 ____
12 ____
13 ____
14 ____
15 ____
16 ____
17 **

18 **Q. Has Ameren Corp taken advantage of this lower downgrade threshold in its financing**
19 **strategies?**

20 A. Yes. Since 2019, Ameren Corp has more than doubled the percentage of holding company
21 debt it uses to finance its subsidiaries (8.39% at June 30, 2019 compared to 18.95% at June
22 30, 2022).[5]

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[4] *Id.,* p. 22, lns. 1-8.
[5] Murray Direct, p. 43, l. 25 – p. 44, l. 3.

1 **Q. Has Ameren Missouri lowered its requested ratemaking common equity ratio in this**
2 **case to recognize the additional debt capacity it supports?**

3 A. No.

4 *FIDUCIARY/CONFLICTS OF INTEREST*

5 **Q. Why would those managing Ameren Corp and its subsidiaries only lobby to relax**
6 **Ameren Corp's credit metrics rather than those used for its subsidiaries?**

7 A. Because, lowering Ameren Corp's cost of capital while maintaining its subsidiaries' higher
8 common equity ratios for ratemaking increases Ameren Corp's shareholders wealth.

9 **Q. Do officers and directors of Ameren Corp's family of companies serve in multiple and**
10 **revolving functions/positions?**

11 A. Yes.

12 **Q. What is Mr. Sagel's position with Ameren Missouri?**

13 A. He is Vice President and Treasurer.

14 **Q. What are Mr. Sagel's positions at Ameren Corp, Ameren Illinois, and ATXI?**

15 A. He is Vice President and Treasurer at each of them.

16 **Q. Does Mr. Sagel having these same financial management positions at each of these**
17 **affiliates raise concerns?**

18 A. Yes. It raises concerns as to his willingness to bargain for the best financial interests of
19 each of these entities at the same time. The fact that Mr. Sagel seems to simply accept that
20 Ameren Missouri has not received any credit for its reduced business risk profile is
21 disturbing. It certainly illustrates to the extent Ameren Missouri does have its own board
22 of directors ("BOD") and officers, they clearly are not looking out for Ameren Missouri's
23 financial interests and the interests of its customers. If Ameren Missouri's interests, and
24 the interests of its ratepayers, were being protected, then Ameren Missouri's officers would

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1 have bargained for Ameren Missouri's rightful debt capacity. As I will demonstrate later,
2 this is even more concerning given that Ameren Missouri's cash flows have supported
3 Ameren Corp's ability to finance its investments in its other subsidiaries as well as paying
4 dividends to Ameren Corp's shareholders over the last several years.

5 **Q. What evidence do you have that Ameren Missouri's officers have not bargained for**
6 **its own independent interests?**

7 A. Ameren Corp's December 17, 2018, presentation to Moody's (Schedule DM-S-2) clearly
8 shows that ** ____
9 ____
10 ____
11 ____
12 ____________________________ **

13 **Q. How do you know that it is Ameren Missouri's reduced business risk that caused**
14 **Moody's to lower its FFO/debt threshold for Ameren Corp?**

15 A. Because Ameren Corp's management made this argument to Moody's in order to convince
16 them that Ameren Corp's FFO/debt threshold should be reduced. Ameren Corp
17 management stated the following during Ameren Corp's Finance Committee Meeting on
18 February 7, 2019:

19 ** ____
20 ____
21 ____
22 ______________ **[6]

23 Ameren Corp management also stated the following during Ameren Corp's Financing
24 Committee Meeting on May 2, 2019:

25 ** ____
26 ____
27 ____

[6] Ameren Corp's Finance Committee Meeting, February 7, 2019, p. 24.

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1 ____
2 ______________________________ **[7]

3 **Q. Did Ameren Missouri argue to Moody's for a lower FFO/debt threshold for purposes**
4 **of the credit rating Moody's assigns to Ameren Missouri's debt?**

5 A. I found no evidence of Ameren Corp performing an analysis on Ameren Missouri's behalf,
6 or Ameren Missouri performing this analysis on its own behalf, to compare Ameren
7 Missouri's FFO/debt metrics to those of its peers in order to attempt to persuade Moody's
8 to reduce Ameren Missouri's FFO/debt threshold.

9 **Q. Who presented information to the rating agencies on behalf of Ameren Corp, Ameren**
10 **Missouri, and Ameren Illinois?**

11 A. According to a December 2018 rating agency presentation, Marty Lyons, Bruce Steinke
12 and Darryl Sagel made the presentation.

13 **Q. Were they officers of Ameren Corp at the time?**

14 A. Yes. Marty Lyons was Executive Vice President and Chief Financial Officer; Bruce
15 Steinke was Senior Vice President, Finance and Chief Accounting Officer; and Darryl
16 Sagel was Vice President and Treasurer.

17 **Q. Did they have the same positions at Ameren Missouri and Ameren Illinois at that**
18 **time?**

19 A. Yes.

20 **Q. Were they employees of Ameren Corp, Ameren Missouri, or Ameren Illinois at the**
21 **time?**

22 A. No. Ameren Services Corporation employed each of these individuals. It still does.

[7] Ameren Corp's Finance Committee Meeting, May 2, 2019, p. 87

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1 **Q. Were any officers solely representing Ameren Missouri for purposes of the rating**
2 **agency presentation?**

3 A. No.

4 **Q. With regard to Ameren Missouri's capital structure in this case, what do you**
5 **conclude based on the foregoing?**

6 A. The only way to ensure Ameren Missouri's ratepayers are given their due consideration
7 for providing the Company more certain cost recovery from PISA, which allows for higher
8 debt capacity, is to adjust Ameren Missouri's common equity ratio to be consistent with
9 that of Ameren Corp's on a consolidated basis. This is the level at which Ameren Corp is
10 balancing its business risk and financial risk to achieve a lower cost of capital and still
11 maintain a reasonably stable investment grade credit rating. Adopting a capital structure
12 consistent with Ameren Corp's consolidated capital structure ensures Ameren Missouri's
13 ratepayers receive the benefit of the additional debt capacity made possible through recent
14 utility-friendly legislation passed in Missouri. Although Mr. Sagel acknowledges that
15 Ameren Missouri's ability to elect PISA was at least the tipping point for Ameren Corp
16 being allowed a more leveraged profile, he stands firm in not giving any consideration to
17 Ameren Missouri's customers in the form of a more leveraged and cost efficient capital
18 structure. In my opinion, this is one of the clearest examples of the need for the
19 Commission to assert its authority to ensure a fair and reasonable outcome for ratepayers.
20 Otherwise, Ameren Corp's shareholders are unfairly enriched through the use of Ameren
21 Missouri's ratepayer-supported debt capacity.

22 **Q. Do you know of any other reason why Ameren Corp management would not push for**
23 **reducing Moody's FFO/debt thresholds for Ameren Missouri?**

24 A. Yes. Ameren Missouri's FFO/debt ratios had typically been more consistent with that of
25 'A' rated credit rather than 'Baa' credit.[8]

[8] Moody's Credit Opinion, Union Electric Company, September 13, 2021, p. 8.

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Q. What Stand-Alone Credit Profile ("SACP") has S&P assigned to Ameren Missouri in the past?

A. Until September 2019, S&P assigned Ameren Missouri a SACP of an 'A-', but it was ultimately assigned a 'BBB+' due to its affiliation with Ameren Corp.

Q. Why did S&P assign Ameren Missouri a stronger SACP?

A. Primarily because of Ameren Missouri's healthier financial risk profile, e.g. higher FFO/debt ratios. However, because Ameren Corp did not have as strong of a financial risk profile ("FRP"), Ameren Missouri's S&P credit rating was limited to a 'BBB+'.

Q. Did Ameren Missouri's stronger FRP provide credit support to Ameren Corp when Ameren Corp financially supported ATXI and AIC?

A. Yes. During the period in which Ameren was supporting investment in ATXI and AIC, Ameren Missouri's FFO/debt ratios were around 24% or higher, which was significantly above the 19% FFO/debt threshold required to maintain a 'Baa1' credit rating. Ameren Missouri could have issued more debt during this period and still had a comfortable FFO/debt margin above 19%. However, if Ameren Missouri had done so, it would have caused Ameren Corp's consolidated FFO/debt ratio to be lower. Maintaining a higher FFO/debt ratio at Ameren Corp over this period was important for Ameren Corp because it was regularly accessing the capital markets, such as to issue commercial paper, in order to fund investment in ATXI, which required significant amounts of capital. After accumulating a significant amount of short-term debt at Ameren Corp due to its investment in ATXI and its refinancing of a $425 million long-term bond, Ameren Corp issued $700 million of bonds in 2015, which was a year in which Ameren Missouri had a FFO/debt ratio of 26.7%[9]. This compared to Ameren Corp's consolidated FFO/debt ratio of 24.4% during the same year.[10]

[9] Moody's Credit Opinion, Union Electric Company, March 29, 2019, Exhibit 2, p. 2.
[10] Moody's Credit Opinion, Ameren Corporation, March 29, 2019, Exhibit 2, p. 2.

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1 **Q. Have Ameren Corp's business and financial risks impaired Ameren Missouri's**
2 **financing flexibility in the past?**

3 A. Yes. Ameren Missouri was foreclosed access to commercial paper markets in August 2008
4 due to the downgrade of its Moody's short-term credit rating to P-3. Ameren Missouri's
5 short-term rating was downgraded due to Moody's downgrading Ameren Corp's long-term
6 rating to 'Baa3'. This downgrade was primarily caused by financial difficulties at Ameren
7 Missouri's affiliates. Because S&P already rated Ameren Corp at a 'BBB-', which meant
8 Ameren Missouri was also rated 'BBB-', Ameren Missouri had an A-3 short-term rating.
9 These Tier-3 short-term ratings foreclosed Ameren Missouri's access to short-term credit
10 markets, which proved to be quite costly to Ameren Missouri ratepayers because of
11 liquidity concerns. Ameren Missouri ratepayers were charged for carrying costs due to the
12 delay in construction at Ameren Missouri's Sioux Scrubber plants.

13 **Q. Why do you conclude that these downgrades foreclosed Ameren Missouri's ability to**
14 **access commercial paper?**

15 A. Because Evergy Metro (f/k/a Kansas City Power & Light Company) had at least one Tier-
16 2 rating, it was able to continue to issue commercial paper to fund its Iatan 2 plant
17 construction during the period of the financial crisis in 2008 to 2009.

18 **Q. Exactly what point are you making by discussing circumstances from over a decade**
19 **ago?**

20 A. I am illustrating the hypocrisy of Mr. Sagel's expressed concerns about Ameren Missouri's
21 ratepayers paying a higher ROR to provide financial stability for a parent company that
22 hasn't always reciprocated. If Ameren Corp desires Ameren Missouri's ratemaking equity
23 ratio to be set at 52%, then Ameren Corp should issue more equity and less debt in order
24 achieve an equity ratio more consistent with the 52% it apparently considers important for
25 financial flexibility.

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1 *OTHER MISSOURI UTILITY COMPANIES' FINANCIAL RISK PROFILES*

2 **Q. Are you aware of other utilities the Commission should consider when evaluating**
3 **Ameren Corp's arguments that Ameren Missouri's assets cannot support more debt**
4 **and lower FFO/debt ratios?**

5 A. Yes. The Commission should consider the ratings treatment given to Missouri's other
6 major electric utility companies, Evergy Metro and Evergy Missouri West.

7 **Q. What is Evergy Metro's current Moody's rating?**

8 A 'Baa1,' which is the same as Ameren Missouri's.

9 **Q. What have Evergy Metro's FFO/debt ratios been the last five years?**

10 A. 19.9% in 2021, 18.8% in 2020, 17.8% in 2019, 18.7% in 2018 and 18.2% in 2017.[11]

11 **Q. Has Evergy Metro been placed on a "negative watch" or even a more general**
12 **"negative outlook" because its FFO/debt ratios had consistently been below the 19%**
13 **threshold Mr. Sagel claims Ameren Missouri is required to maintain to avoid being**
14 **downgraded by Moody's?**

15 A. No. Evergy Metro currently has a "stable outlook" despite its FFO/debt ratio being below
16 19% for four of the last five years. Moody's indicates that it expects Evergy Metro's
17 FFO/debt ratios to be in the "high teens" for the next 12-18 months. Moody's indicates it
18 may consider a downgrade if Evergy Metro's FFO/debt falls below 18% on a sustained
19 basis.

20 **Q. Are you aware of any compelling reason why Moody's should view Evergy Metro's**
21 **and Ameren Missouri's financial risk thresholds differently?**

22 A. No.

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[11] Moody's Credit Opinion, Evergy Metro Inc., April 29, 2021, p. 3.

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1 **Q. What was Evergy Metro's last authorized capital structure for purposes of setting its**
2 **allowed ROR?**

3 A. In Evergy Metro's (f/k/a Kansas City Power & Light Company) last fully litigated rate
4 case, Case No. ER-2016-0285, the Commission authorized Evergy Metro a ratemaking
5 capital structure consisting of 49.2% common equity and 50.8% long-term debt.

6 **Q. Did any rating agency put Evergy Metro on a "negative watch" or "negative outlook"**
7 **after the Commission authorized that capital structure?**

8 A. No.

9 **Q. Did Evergy Metro recommend an equity ratio similar to that which the Commission**
10 **authorized?**

11 A. Yes. Evergy Metro recommended a common equity ratio of 49.72%.

12 *COMPARISON TO AMEREN ILLINOIS' CAPITAL STRUCTURE*
13 *ARGUMENTS BEFORE THE ILLINOIS COMMERCE COMMISSION*

14 **Q. Mr. Sagel warns of potential negative credit and cost of capital ramifications if the**
15 **Commission were to authorize Ameren Missouri a lower common equity ratio than**
16 **that shown on Ameren Missouri's books.[12] Did Ameren Illinois witnesses raise the**
17 **same warning to argue for a higher authorized common equity ratio for purposes of**
18 **implementing its electric utility rates after it was allowed to use formula rates starting**
19 **in 2012?**

20 A. Yes. Subsequent to Illinois' passage of the Energy Infrastructure Modernization Act in
21 2011, Ameren Illinois began filing annual rate cases for its electric utility in Illinois. Over
22 the course of approximately three years, Ameren Illinois and ICC Staff vigorously debated
23 a fair and reasonable ratemaking common equity ratio in which to apply the formula ROE
24 of 580 basis points plus a 12-month average 30-year United States Treasury yield. The

[12] Sagel Rebuttal, p. 24, ll. 6-19.

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1 arguments in the Ameren Illinois rate cases were quite similar to those in this case. Ameren
2 Illinois' witnesses asserted Ameren Illinois had to maintain a higher common equity ratio
3 in order to offset higher business risks associated with the Illinois regulatory
4 environment.[13]

5 **Q. What ratemaking common equity ratio did Ameren Illinois recommend in the**
6 **inaugural case (2012) pursuant to Illinois' Energy Infrastructure Modernization Act?**

7 A. 54.297% in Docket No. 12-0001.[14]

8 **Q. What equity ratio did the Illinois Commerce Commission (ICC) Staff witness**
9 **recommend in that case?**

10 A. 51.49%.

11 **Q. What did the ICC authorize?**

12 A. 51.49%.

13 **Q. What common equity ratio did Ameren Illinois recommend for its electric utilities in**
14 **its 2013 rate case, Docket No. 13-0301?**

15 A. 54.62%.

16 **Q. What common equity ratio did the ICC Staff recommend?**

17 A. 51%.

18 **Q. What was the premise for ICC Staff's recommended common equity ratio?**

19 A. Ameren Corp's average consolidated common equity ratio for 2011.

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[13] Illinois Docket No. 12-001, Ryan J. Martin Rebuttal Testimony, p. 5, l. 97 through p. 6, l. 116.
[14] Illinois Docket No. 12-0001, Schedule D-1 Sponsored by Ryan J. Martin

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1 **Q. What common equity ratio did the ICC authorize in that case?**

2 A. 51%.

3 **Q. What common equity ratio did Ameren Illinois recommend for its electric utilities in**
4 **its 2014 rate case, Docket No. 14-0317?**

5 A. 51%.

6 **Q. What about the ICC Staff?**

7 A. 51%.

8 **Q. Why did they recommend the same common equity ratio?**

9 A. Because the ICC Staff and Ameren Illinois had agreed to use a 51% common equity ratio
10 for purposes of that case.

11 **Q. Did they agree to use that same equity ratio in subsequent cases?**

12 A. No. They agreed to use a 50% common equity ratio, which was later codified as an
13 amendment to the Energy Infrastructure Modernization Act.

14 **Q. Over the period of all of these cases in which Ameren Illinois' fair and reasonable**
15 **ratemaking capital structure was debated and decided by the ICC, were Ameren**
16 **Illinois' credit ratings put on a negative outlook or watch?**

17 A. No.

18 *PRO FORMA IMPACT OF CAPITAL STRUCTURE ON CREDIT PROFILE*

19 **Q. Did Mr. Sagel quantify the potential impact the Commission's adoption of your**
20 **capital structure recommendation may have on Ameren Missouri's FFO/debt ratios?**

21 A. Yes. Mr. Sagel estimates that if Ameren Missouri's revenue requirement in 2021 had been
22 premised on my recommended capital structure containing a 43% common equity ratio,

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1 this would cause Moody's FFO/debt ratio to be approximately 14.0%.[15] This compares to
2 the 18.4% actual FFO/debt achieved by Ameren Missouri in 2021.[16]

3 **Q. Do you agree with his *pro forma* estimates?**

4 A. No.

5 **Q. What about his methodology?**

6 A. His methodology is reasonable.

7 **Q. Why do you disagree with his estimates?**

8 A. Mr. Sagel calculated his *pro forma* adjustments based on Ameren Missouri's total capital
9 and rate base as of December 31, 2022. Because Ameren Missouri's 2021 FFO/debt ratios
10 are premised on rates in effect for 2021, the *pro forma* adjustments should be calculated
11 based on parameters used to determine the rates in effect in 2021. These parameters were
12 determined in Ameren Missouri's 2019 rate case, Case No. ER-2019-0335. Ameren
13 Missouri's total capital was about $4 billion less as of the true-up date, December 31, 2019
14 as compared to December 31, 2022. Ameren Missouri's electric utility rate base was
15 approximately $3.5 billion lower.

16 Because the parties did not specify an underlying capital structure or ROR in their black
17 box stipulation and agreement in the 2019 rate case, the capital structure supporting 2021
18 rates is ambiguous. Staff had recommended a 50% common equity ratio, OPC
19 recommended a 48% common equity ratio, and Ameren Missouri recommended a 51.93%
20 common equity ratio. For sake of estimating the potential largest *pro forma* impact on
21 Ameren Missouri's 2021 FFO, I estimated the *pro forma* impact on Ameren Missouri's
22 2021 FFO by applying the full difference of Ameren Missouri's recommended 51.93%

[15] Sagel Rebuttal, p. 24, l. 1 – p. 37, l. 8.
[16] Moody's Credit Opinion, Union Electric Company, September 29, 2022, Exhibit 1, p. 2.

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1 equity ratio to a 43% equity ratio. I estimate that Ameren Missouri's FFO/debt ratios
2 would have been 15.2% compared to the actual of 18.4%.

3 **Q. What FFO/debt ratios does Moody's expect for Ameren Missouri on a going forward**
4 **basis?**

5 A. Approximately 20%.[17]

6 **Q. If the Commission set Ameren Missouri's ROR based on your recommended capital**
7 **structure, what impact would the approximate 3% reduction to Ameren Missouri's**
8 **FFO/debt ratio have on Ameren Missouri's projected FFO/debt ratios?**

9 A. They would be approximately 17%, which is consistent with the threshold Ameren Corp
10 bargained for itself from Moody's.

11 **Q. Would this not cause Ameren Corp's FFO/debt ratios to be lower than Ameren**
12 **Missouri's FFO/debt ratios?**

13 A. Only if Ameren Corp maintains the current proportion of holding company debt in its
14 consolidated capital structure.

15 *PARENT/SUBSIDIARY FINANCING RELATIONSHIP*

16 **Q. Does an increasing amount and percentage of holding company debt cause financial**
17 **instability for the entire Ameren Corp enterprise?**

18 A. Yes. S&P Global Ratings clearly states that Ameren Missouri does not have sufficient
19 insulation mechanisms in place to allow it to have a separate and distinct credit rating from
20 Ameren Corp. Therefore, Ameren Corp's financial and business risks impact the rating
21 S&P Global Ratings assigns to Ameren Missouri.

[17] *Id.*

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1 **Q. Have other jurisdictions denied proposed acquisitions due in part to the financial**
2 **instability that would be caused by issuing too much holding company debt to fund**
3 **the acquisition?**

4 A. Yes. This was one of the factors the Kansas Corporation Commission's ("KCC") cited in
5 its disapproval of Great Plains Energy's proposed acquisition of Westar Energy.

6 **Q. Great Plains Energy and Westar Energy merged did they not?**

7 A. Yes, but only after they restructured the transaction to be a merger of equals ("MOE"),
8 which is essentially a transaction in which each company's shareholders swap their shares
9 for a pro-rated ownership interest in the combined company. Unlike the initial proposed
10 transaction, this type of transaction did not involve use of leverage at the holding company.

11 **Q. Did the KCC impose any conditions on the merger to control the potential of Evergy**
12 **issuing a disproportionate share of holding company debt to leverage its returns after**
13 **the merger closed?**

14 A. Yes. A condition of the KCC's approval of the merger was to institute an Earnings Review
15 and Sharing Plan ("ERSP"). The KCC understood that the newly formed entity, Evergy,
16 could attempt to retain more earnings for shareholders by using more debt leverage at the
17 holding company level as compared to its subsidiaries. Consequently, to the extent
18 Evergy's consolidated common equity ratio was lower than its subsidiaries' common
19 equity ratios by 2.5% to 3.5%, the percentage of equity allowed to be counted for the ERSP
20 would be reduced by a proportionate amount.

21 **Q. How much lower is Ameren Corp's equity ratio than Ameren Missouri's common**
22 **equity ratio?**

23 A. As shown in Schedule DM-S-1, pages 5 and 8, attached to this testimony, the difference
24 between Ameren Cop's common equity ratio and Ameren Missouri's common equity ratio
25 has been expanding over the last several years, with it recently reaching an approximate
26 ten percentage point difference on September 30, 2022.

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1 **Q. What common equity ratio did the KCC allow Evergy's subsidiaries for purposes of**
2 **the ERSP?**

3 A. 51% in 2019, 50.5% in 2020 and 50% in 2021 through 2022.

4 **Q. What common equity ratios has Evergy maintained in recent periods?**

5 A. Evergy's common equity ratios has been in the range of 47% to 48%.

6 **Q. When describing your recommended capital structures in utility rate cases over the**
7 **last several years, Ms. Bulkley indicates that you have not recommended a common**
8 **equity ratio over 48%.[18] Why not?**

9 A. Because almost all of Missouri's utilities are owned by parent companies that use holding
10 company debt to leverage their returns. The highest common equity ratio I recommended
11 was in the recent Evergy Metro and Evergy Missouri West rate cases, Case Nos. ER-2022-
12 0129 and ER-2022-0130, respectively. Evergy Inc. has not issued as much holding
13 company debt as other Missouri utilities because as I explained earlier in my testimony,
14 the Kansas Corporation Commission ("KCC") imposed limitations on Evergy's use of
15 holding company debt for purposes of its ERSP.

16 **Q. What is Ameren Corp's consolidated common equity ratio?**

17 A. Around 42% to 43% without short-term debt, and around 40% with short-term debt.
18 Ameren Corp's common equity ratio has declined from 48% in 2019, 45% in 2021 to its
19 current level.

20 **Q. Do investors believe that this Commission's potential consideration of Ameren Corp's**
21 **use of holding company debt in setting Ameren Missouri's ROR constrains Ameren**
22 **Corp from being even more aggressive in its use of holding company debt?**

23 A. Yes. Wells Fargo stated the following in a recent report on Ameren Corp:

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[18] *Id.,* p. 60, lines 12-13.

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1 AEE's '23-27 new equity needs total $2.8B, consisting of $2.3B of external equity
2 and $100M annually under DRPlus [dividend reinvestment plan] and internal
3 programs. AEE continues to target a parent equity ratio of ~45%. The equity
4 guidance is consistent with our assumption and '23 needs of $0.4B represent ~1.5%
5 of market cap. **AEE employs a relatively conservative financing strategy vs.
6 peers, likely reflecting regulatory-related look-through considerations in MO.**
7 (emphasis added)[19]

8 **Q. Mr. Sagel testifies that equity infusions in Ameren Missouri are traceable to Ameren
9 Corp external equity issuances, and therefore because this is the capital that supports
10 Ameren Missouri's rate base, this is the capital structure that should be used for the
11 authorized ROR.[20] First, do you agree that tracing the capital to external issuances
12 should be the determining factor for assessing a fair and reasonable capital structure?**

13 A. No. Ameren Corp's equity issuances benefit the entire enterprise's credit profile, not just
14 Ameren Missouri's credit profile. A recognized principle of finance is that it is the risk of
15 the investment that determines the cost of capital, not the source of funds. Based on Mr.
16 Sagel's logic, if Ameren Corp only sourced third-party equity for equity infusions into
17 Ameren Missouri, but issued holding company debt to infuse equity into its other
18 subsidiaries, only Ameren Missouri's capital structure would be legitimate. It is this type
19 of logic that supports S&P's family ratings approach to assigning credit ratings based on
20 the parent company's consolidated credit profile.

21 **Q. Mr. Sagel asserts that you suggest in your direct testimony that Ameren Missouri's
22 dividend payout ratio should be similar to Ameren Corp's.[21] Is he correct?**

23 A. No. I asserted in my testimony that if Ameren Missouri were managed as if it were a stand-
24 alone entity, it would have a carefully managed dividend payment policy, similar to how
25 Ameren Corp manages its targeted dividend payout ratio in the range of 55% to 70%.

[19] Neil Kalton, et. al., "AEE: Quick Take on Q4 Updates – All Looks Just Fine," Wells Fargo, February 15, 2023.
[20] Sagle Rebuttal, p. 9, lns. 5-16.
[21] Sagel Rebuttal, p. 11, l. 1 – p. 12, l 13.

1 **Q. What did you intend to convey?**

2 A. That if Ameren Missouri were a stand-alone entity, as it was prior to the formation of
3 Ameren Corp in 1997 as the holding/parent company of Ameren Missouri and its affiliates,
4 it would be expected to fund a consistent quarterly dividend to third party shareholders.
5 As a stand-alone entity accountable to third-party shareholders, it would be obligated to
6 fund the dividend regardless of its cash flow position (i.e. free cash flow negative due to
7 increased investment needs or free cash flow positive due to reduced investment needs).

8 **Q. Mr. Sagel testifies that the fact that Ameren Corp "had to lean more on parent**
9 **company debt" to fund dividends during Ameren Missouri's current capital intensive**
10 **spending cycle shows Ameren Missouri's financial independence as it relates to**
11 **managing its capital structure in a responsible and prudent manner as its cash flow**
12 **position has changed.[22] Do you agree?**

13 A. No. First, I take issue with Mr. Sagel's characterization that Ameren Corp had to "lean
14 more on parent company debt" to fund dividends. Ameren Corp did not have to "lean more
15 on parent company debt" to fund dividends, it chose to. Ameren Corp's ability to issue
16 debt is a function of its ownership of its regulated utility subsidiaries. Ameren Corp has
17 no assets other than its regulated utility subsidiaries. Its balance sheet capacity is dependent
18 on its low-risk regulated utilities, not independent of such. Again, as I described in my
19 direct testimony, Ameren Corp's sharing of credit facilities with Ameren Missouri and
20 Ameren Illinois allow it access to commercial paper markets. Ameren Corp's officers and
21 Board of Director's decision to issue commercial paper at the holding company rather than
22 at Ameren Missouri to fund third-party dividends is a matter of choice, not need.

23 Second, if Ameren Corp were a third-party shareholder of Ameren Missouri, similar to
24 shareholders of Union Electric prior to 1997, it would expect a consistent quarterly
25 dividend from Ameren Missouri despite Ameren Missouri's cash flow position. As
26 demonstrated by Union Electric's consistent and growing dividends while it built the
27 Callaway Nuclear Plant in the late 1970s and early 1980s. During this period, not only did

[22] Sagel Rebuttal, p. 12, lines 3-13.

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1 Union Electric maintain the dividends paid to third-party shareholders, but its dividends
2 increased at a CAGR of approximately 3.2%. Because Union Electric was truly an
3 independent entity responsible to third-party shareholders, it issued its own short-term debt
4 to finance its construction needs while still maintaining investors' expected dividends.

5 Third, an analysis of Ameren Corp's and Ameren Missouri's capital flows during the fourth
6 quarter of 2022 proves Mr. Sagel's arguments are wrong. Mr. Sagel testifies that Ameren
7 Corp has financed Ameren Missouri's portion of dividends for the last couple of years
8 because Ameren Missouri needs to retain capital for reinvestment. I agree that Ameren
9 Missouri is currently cash flow negative due to its current intensive capital expenditure
10 cycle. Ameren Missouri's situation did not suddenly change during the fourth quarter of
11 2022. Ameren Missouri's operations generated $404 million of positive cash flow during
12 the fourth quarter of 2022, but because Ameren Missouri spent $448 million on
13 investments, it needed capital to finance its cash deficiency. Based on Mr. Sagel's claim
14 that Ameren Corp is covering Ameren Missouri's dividend contributions, Ameren
15 Missouri should not have distributed a dividend to Ameren Corp during the fourth quarter
16 of 2022. Not only did Ameren Missouri need capital to fund its investment obligations, it
17 also needed capital to repay $55 million of long-term debt. However, instead of retaining
18 Ameren Missouri's $15 million of fourth quarter earnings, it actually distributed over 3
19 times its fourth quarter 2022 earnings ($46 million) as dividends to Ameren Corp.

20 **Q. Based on your analysis of Ameren Corp's and Ameren Missouri's financial**
21 **statements, how was the amount of Ameren Missouri's dividend distribution to**
22 **Ameren Corp determined?**

23 A. By targeting a common equity ratio requested for ratemaking. The true-up date in this case
24 is the period ended December 31, 2022. As Mr. Sagel testified in his direct testimony, he
25 projected a 51.93% common equity ratio for Ameren Missouri at the end of the true-up
26 period. Based on Ameren Missouri's capital balances at the end of the true-up period, its
27 common equity ratio is almost exactly at 51.93% (51.91% based on my Schedule DM-S-
28 1, p. 7). If Ameren Missouri had not distributed $46 million of dividends to Ameren Corp,
29 its common equity ratio would have been 52.09%.

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1 **Q. Did Dr. Won testify in rebuttal that he was not aware that Ameren Corp targeted a**
2 **common equity ratio of approximately 52% for Ameren Missouri?**

3 A. Yes. Dr. Won cites Mr. Sagel's response to Data Request No. 0192 when he testifies as
4 follows:

5 Interestingly, according to Ameren Missouri, it has neither internally
6 identified nor externally communicated a targeted capital structure.[23]

7 **Q. Did you provide information to Dr. Won to support the fact that Ameren Corp.**
8 **targets a 52% ratemaking common equity ratio for Ameren Missouri?**

9 A. Yes. See my attached response to Dr. Won's DR No. 476 (Schedule DM-S-3). In my
10 response I directed Dr. Won to page 48 of an Ameren Corp rating agency presentation
11 (attached as Schedule DM-S-4) Ameren Missouri provided to Staff in response to its DR
12 No. 190. I also directed Dr. Won to Mr. Sagel's Direct Testimony which states that Ameren
13 Missouri's equity ratio has been managed to a target of around 52%.

14 **Q. Is it possible that Ameren Missouri could have "leaned on" Ameren Corp to issue**
15 **short-term debt to fund the $46 million dividend payment?**

16 A. Yes. In fact, Ameren Corp's short-term debt balance declined by $153 million during the
17 fourth quarter of 2022 so it could have used holding company debt to "assist" Ameren
18 Missouri.

19 **Q. Do the capital flows between Ameren Corp and Ameren Missouri establish that**
20 **Ameren Missouri's capital structure is not the result of arms-length transactions?**

21 A. Yes. I agree with Mr. Sagel's testimony about the basic financial principle that the "use of
22 funds invested gives rise to the risk of the investment."[24] The purest insight as to Ameren
23 Corp's view about the business risk associated with investing in its regulated utility
24 subsidiaries is the capital structure it maintains at the consolidated level. It is this capital
25 structure that has the competing interests of achieving the lowest reasonable cost of capital,

[23] Won Rebuttal, p. 10, lines 10-12.
[24] Sagel Rebuttal, p. 8, ll. 4-7.

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1 while at the same time maintaining an equity layer that ensures financial stability of the
2 entire enterprise. If Ameren Corp wants its utilities' ratepayers to pay for a more costly
3 equity-rich capital structure, it should issue more common equity at the holding company
4 level which would provide ratepayers with the benefit of a more financially sound parent
5 rather than the current situation in which Ameren Corp's higher leverage is a credit
6 constraint.

7 **Q. Does the basic financial principle that the required return is related to the use of the**
8 **funds and not the source of the funds also contradict Mr. Sagel's claim that Ameren**
9 **Missouri's capital structure is legitimate because the equity shown on its balance**
10 **sheet was funded by equity issued by Ameren Corp?**

11 A. Yes. Mr. Sagel's attempt to claim that Ameren Missouri's per books capital structure is
12 legitimate because the source of Ameren Missouri's equity infusion was third-party
13 common equity issued by Ameren Corp, contradicts his own position that it is the use of
14 the funds and not the source of the funds that influences the cost of capital. I agree that it
15 is the risk of the underlying investment that drives the cost of capital and determines the
16 amount of debt leverage that can reasonably be used. Ameren Corp's more leveraged
17 capital structure captures managements' view of the debt capacity of its low-risk regulated
18 utility assets.

19 **Q. Has Mr. Sagel testified in the past that Ameren Missouri needed more common equity**
20 **than Ameren Illinois because it is an integrated-electric utility while Ameren Illinois**
21 **is a distribution-only utility?**

22 A. Yes. As recently as Ameren Missouri's 2019 rate case, Mr. Sagel testified as follows in
23 his rebuttal testimony:

24 Given the higher-risk nature of Ameren Missouri's vertically-integrated
25 business, (with numerous energy centers including one nuclear center)
26 relative to the risk of Ameren Corporation's other primary subsidiaries
27 (Ameren Illinois operates electric transmission and distribution facilities
28 and natural gas delivery facilities), it stands to reason that Ameren Missouri

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1 would support and maintain a common equity ratio that is higher than
2 Ameren Corporation's consolidated equity ratio.[25]

3 and

4 The lower overall risk profile of Ameren Illinois relative to Ameren
5 Missouri is also evident in Ameren Illinois' stronger issuer rating at
6 Moody's, which rates Ameren Illinois A3 and Ameren Missouri Baa1.
7 Moody's ratings for each of Ameren Illinois and Ameren Missouri are
8 independently developed based on their discrete credit profiles.[26]

9 **Q. What are Ameren Illinois' and Ameren Missouri's current Moody's credit ratings?**

10 A. Moody's still rates Ameren Illinois one notch higher at 'A3' as compared to Ameren
11 Missouri's 'Baa1' rating.

12 **Q. What was Ameren Illinois' ratemaking common equity ratio at the time Mr. Sagel**
13 **argued Ameren Illinois' capital structure should be managed to a lower common**
14 **equity ratio due to the lower risk profile of its operations?**

15 A. 50%.

16 **Q. What common equity ratio does Mr. Sagel suggest should now be used for purposes**
17 **of setting Ameren Illinois' rate of return in its recently filed multi-year rate plan**
18 **request before the Illinois Commerce Commission ("ICC")?**

19 A. Mr. Sagel sponsored capital structure testimony on January 20, 2023, before the ICC where
20 he requested that Ameren Illinois electric utility rates be set based on a 54% common equity
21 ratio over the four year period of the multi-year rate plan.[27]

22 **Q. What is ATXI's per books common equity ratio?**

23 A. 60%.

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[25] Case No. ER-2019-0335, Darryl T. Sagel Rebuttal, p. 14, lines 3-8.
[26] *Id.,* p. 31, lines 5-8.
[27] Ameren Illinois Company Petition for Approval of a Multi-Year Rate Plan pursuant to 20 ILCS 5/16-108.18, Docket No. 23-0082, Darryl T. Sagel Direct, January 20, 2023 - Document for 23-0082 (illinois.gov)

1 **Q. Is ATXI's common equity ratio consistent with Mr. Sagel's testimony that Ameren**
2 **Missouri's affiliates can incur a higher percentage of debt because of lower business**
3 **risk?**

4 A. No. Despite the fact Ameren Corp's ATXI subsidiary has the lowest business risk of its
5 three primary operating subsidiaries, its balance sheet implies it requires the highest
6 common equity ratio. The fact that this is clearly not true provides further evidence that
7 Mr. Sagel's testimony is not credible.

8 **Q. Can you provide corroborating evidence which demonstrates that ATXI is considered**
9 **to be Ameren Corp's lowest-risk subsidiary?**

10 A. Yes. Both Moody's and S&P consider transmission-only companies subject to FERC rate
11 regulation to have the least amount of business risk of most utility subsectors, with the only
12 exception being water utility companies. S&P assesses the financial risk of transmission-
13 only companies, such as ATXI, against low-volatility benchmarks as compared to medial
14 volatility benchmarks for vertically-integrated electric utility companies. In Moody's most
15 recent report assessing the risk profiles of Ameren Corp's subsidiaries, it ranked ATXI as
16 having the least business risk of all of its subsidiaries with Ameren Missouri ranked third
17 after Ameren Illinois.

18 Additionally, Wall Street equity analysts typically assign the highest P/E multiples to
19 FERC-regulated transmission earnings because of the low-risk nature of these assets.

20 **Q. Considering the general rank-order of Ameren Corp's subsidiaries' business-risk**
21 **profiles, why are the targeted common equity ratios the opposite of Mr. Sagel's**
22 **explanation of basic risk and return principles?**

23 A. Because the subsidiaries' capital structures are primarily managed for ratemaking
24 purposes, not achieving the lowest reasonable cost of capital consistent with the underlying
25 business risk.

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1 **Q. How can this Commission ensure Ameren Missouri's ratepayers are charged for a**
2 **market-driven capital structure rather than a ratemaking-driven capital structure?**

3 A. Consider Ameren Corp's consolidated capital structure strategies. This is the only capital
4 structure that has the competing interest of being managed to achieve a lower cost of capital
5 for the benefit of its shareholders while also minimizing the issuance of additional third-
6 party common equity to reduce dilution of earnings to existing shareholders. If Ameren
7 Corp desires to be awarded a ROR consistent with Ameren Missouri's higher-cost capital
8 structure, then it should issue additional common equity to third-party equity investors.

9 *INVESTOR EXPECTATIONS ON RATEMAKING CAPITAL STRUCTURE*

10 **Q. Mr. Sagel discusses market responses to the Commission's deliberations in the Spire**
11 **Missouri gas rate cases, Case Nos. GR-2017-0215 and GR-2017-0216, in an effort to**
12 **justify why the Commission should accept Ameren Missouri's proposed capital**
13 **structure.[28] Do you think market response like these should be the Commission's**
14 **primary focus when making rates?**

15 A. No. While even as a consumer advocate witness, I do consider the potential impact on a
16 company's investors when making my recommendations; a negative stock price reaction
17 is not proof of a bad Commission decision. Investors' expectations are impacted by many
18 different factors, with anticipated Commission decisions being one of the primary factors.
19 Investors price in the probability of expected outcomes in rate cases. If a particular
20 commission has consistently awarded higher ROEs with equity-rich capital structures,
21 investors price in these investor-friendly outcomes in their projections. Additionally,
22 companies' guidance regarding discrete EPS expectations as well as guidance on long-term
23 compound annual growth rates ("CAGR") in EPS greatly influences investors'
24 expectations. Ameren Corp has consistently guided investors to an expectation of a 6% to
25 8% long-term CAGR in EPS. However, this earnings guidance has many assumptions
26 underlying it. The key factors typically influencing the earnings guidance of a pure-play
27 regulated utility such as Ameren Corp are anticipated rate base growth, the probability of

[28] Sagel Rebuttal, p. 39, l. 14 – p. 42, l. 13.

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recovery of this increased investment, and the parameters applied to the rate base for purposes of allowed returns (which include an assumed capital structure and potential allowed ROEs). ** ______

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______ ** As I explained in Spire Missouri's recent 2022 rate case, Case No. GR-2022-0179, because Spire Inc. guided investors to expect Spire Missouri's rates be set at a 54% common equity ratio, it was no surprise that Spire Inc.'s stock price declined when the Commission ordered a lower ROR based on a capital structure with a lower common equity ratio. A stock price decline should not be viewed as an unfair outcome, but rather an outcome that is different from investors' expectations.

FOUR CRITERIA – SUBSIDIARY VS. PARENT CAPITAL STRUCTURE

Q. Do Dr. Won and Mr. Sagel cite similar criteria to support their view that Ameren Missouri's per books capital structure is appropriate for setting Ameren Missouri's ROR in this case?

A. Yes. Both Dr. Won and Mr. Sagel believe the following criteria support their argument to use Ameren Missouri's per books capital structure to set its authorized ROR:

1. Whether the subsidiary utility obtains all of its capital from its parent, or issues its own debt and preferred stock;
2. Whether the parent guarantees any of the securities issued by the subsidiary;
3. Whether the subsidiary's capital structure is independent of its parent (i.e. existence of double leverage, absence of proper relationship between risk and leverage of utility and non-utility subsidiaries);

[29] "Leading the Way to a Sustainable Energy Future," Ameren's Long-Term Strategy, Ameren Board of Directors Discussion, June 9-10, 2022, p. 86.

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4. Whether the parent (or consolidated enterprise) is diversified into non-utility operations.[30]

Mr. Sagel and Dr. Won appear to agree on why they believe the first three criteria support the use of Ameren Missouri's per books capital structure to set its authorized ROR. However, while both witnesses believe the fourth criterion supports the use of Ameren Missouri's capital structure, they have opposite rationales for that belief.

Q. Did you address any aspects of these criteria in your rebuttal testimony?

A. Yes. While Dr. Won did not specifically cite the above-criteria in his direct testimony, he testified about several factors similar to these criteria that he believes supports using Ameren Missouri's capital structure. The factors cited in Dr. Won's direct testimony closely follow Mr. Sagel's response to Dr. Won's Data Request No. 0196 attached as Schedule DM-R-1 to my rebuttal testimony.

Q. Did Dr. Won request an update of Mr. Sagel's response to Staff Data Request No. 0196?

A. Yes. Dr. Won issued Data Request 0196.2 to request Mr. Sagel reaffirm his initial responses to Staff Data Request 0196. Mr. Sagel's response to Dr. Won's Data Request 0196.2 as well as Data Request 0196.1 are attached to this testimony as Schedules DM-S- and DM-S-6, respectively.

Q. How do Mr. Sagel's responses to Dr. Won's data request address the four criteria?

A. As it relates to the first factor, Dr. Won requested Ameren Missouri to either affirm or deny whether it has executed affiliate notes (short-term or long-term) with Ameren Corp (item numbers 1 and 2 in Dr. Won's DR). Other than money pool borrowings, Mr. Sagel denies that Ameren Missouri has executed affiliate notes with Ameren Corp. Therefore, based on Mr. Sagel's response and the fact that Ameren Missouri issues its own long-term and short-

[30] David Parcell, "The Cost of Capital – A Practitioner's Guide," 2010 Edition, p. 46.

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1 term debt, Dr. Won and Mr. Sagel agree that the first factor supports use of Ameren
2 Missouri's capital structure.

3 Although it is a fact that Ameren Missouri issues its own short-term debt and long-term
4 debt, the fact that Ameren Corp shares a credit facility with Ameren Missouri should also
5 be considered. Ameren Missouri's credit quality allows both Ameren Corp and Ameren
6 Missouri to access short-term debt capital markets. As I have testified, it is Ameren Corp's
7 choice to issue short-term debt at the holding company level to fund dividends rather than
8 doing so at Ameren Missouri. Ameren Missouri was able to fund and grow its dividends
9 to third-party investors before Ameren Corp became its holding company.

10 Item numbers 5 and 6 of Dr. Won's DR No. 196 address the second criterion as to whether
11 Ameren Corp guarantees any of Ameren Missouri's debt issuances. I agree with Mr. Sagel
12 and Dr. Won that Ameren Corp does not guarantee Ameren Missouri's debt. However,
13 Ameren Corp derives its creditworthiness from its regulated utilities, which includes
14 Ameren Missouri. As proven by Ameren Corp's startup investment in ATXI, it uses cash
15 flows from its regulated utility subsidiaries to subsidize affiliate capital investment needs.
16 Ameren Corp's ability to issue holding company debt is a function of its ownership of its
17 regulated utilities, including Ameren Missouri. Ameren Corp does so at the expense of
18 Ameren Missouri's credit quality and a higher ROR charged to ratepayers.

19 Dr. Won's Data Request No. 0196.1 to Ameren Missouri relates to the third criterion. As
20 can be seen in Schedule DM-S-6, Dr. Won asked Ameren Missouri whether Ameren Corp
21 issued debt within the last three years for the purposes of purchasing equity in Ameren
22 Missouri. First, in order to verify Mr. Sagel's response, I analyzed Ameren Corp and
23 Ameren Missouri's quarterly cash flow statements since 2020.

24 Although Ameren Corp's equity contributions into Ameren Missouri generally reconcile
25 with the timing of Ameren Corp's issuance of third-party common equity, I discovered
26 other common equity contributions that demonstrate the lack of arms-length financial
27 transactions between Ameren Corp and Ameren Missouri. Specifically, in the fourth
28 quarter of 2020, Ameren Corp contributed $66 million of common equity into Ameren

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1 Missouri only to have it immediately returned to Ameren Corp as a dividend payment.
2 Ameren Corp contributed $24 million of common equity into Ameren Missouri again in
3 the fourth quarter of 2021 only to have it immediately returned as dividends.

4 Although Ameren Missouri has indicated these transactions are related to its consolidated
5 tax allocation agreements, I do not understand the commercial purpose of such zero-sum
6 transactions. Second, consistent with the basic risk and return principle that it is the risk
7 of the investment, and not the cost of the source of the funds that drives an investor's
8 required return, it is inappropriate to focus on whether Ameren Corp's equity infusions into
9 Ameren Missouri are raised with debt or equity financings. The proper focus should be
10 the capital structure that is consistent with the risk profile of Ameren Corp's subsidiaries.
11 Mr. Sagel's argument that Ameren Missouri ratepayers should be charged a ROR based on
12 a 52% common equity ratio because the source of Ameren Missouri's common equity was
13 equity raised by Ameren Corp defies this basic risk/return principle.

14 **Q. Did Ameren Corp contribute any of the funds raised from the December 2020 and**
15 **February 2021 equity issuances to any subsidiaries other than Ameren Missouri?**

16 A. I do not know. While Mr. Sagle testifies that Ameren Missouri received all of the funds
17 raised from Ameren Corp's equity issuance, during this same period Ameren Corp
18 contributed $154 million of common equity into its subsidiary AIC. The total of the equity
19 contributions to Ameren Missouri and AIC for these two quarters is $692 million, which
20 exceeds the $564 million of external common equity Ameren Corp issued for the same
21 period.

22 **Q. If Ameren Corp contributed more equity to its subsidiaries Ameren Missouri and**
23 **AIC than it raised in third-party common equity, how did Ameren Corp raise the**
24 **additional funds it contributed to its subsidiaries?**

25 A. By issuing debt.

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1 **Q. Is this an instance of double leveraging?**

2 A. Yes. Double leveraging occurs when a holding company issues debt in addition to its
3 subsidiaries issuing debt. While Mr. Sagel is attempting to legitimize Ameren Missouri's
4 common equity ratio by maintaining that third-party equity funds are used to fund equity
5 contributions into Ameren Missouri, this argument fails Mr. Sagel's own argument that it
6 is the use of the funds, not the source of the funds that drives a fair and reasonable rate of
7 return. If Ameren Corp viewed the business risks related to its subsidiary investments as
8 high risk, it would not finance its equity investments in its subsidiaries with debt capital.
9 The primary factor driving Ameren Corp's use of holding company debt is that it can
10 achieve a lower cost of capital for investments in its utilities without sharing this lower cost
11 with ratepayers. In Ameren Corp's case, the fact that Ameren Corp only owns regulated
12 utility assets and it has a much more leveraged consolidated capital structure than its
13 subsidiaries, proves that there is an absence of a proper relationship between risk and
14 return. But for Ameren Corp's ownership of low-risk regulated utilities, it would not be
15 able to raise holding company debt.

16 **Q. Is the comparison of Ameren Missouri's business risk to that of its holding company,**
17 **Ameren Corp, the premise of the fourth criterion listed above?**

18 A. Yes. The fourth criterion provides insight as to whether it is logical to expect the parent
19 company's consolidated capital structure to be significantly different than that of its
20 subsidiary due to the parent's consolidated business risk being different than the risk of the
21 subsidiary. The criterion specifically identifies non-utility operations as a consideration
22 because non-utility operations typically have a higher business risk than monopoly utility
23 operations. If a parent company has insignificant non-regulated and/or non-utility
24 operations, then it is not logical for the parent company to have a significantly different
25 capital structure than its subsidiaries.

1 **Q. Did Dr. Won request Ameren Missouri to provide him information as it relates to the**
2 **last criterion?**

3 A. Yes. Item No. 8 of Dr. Won's Data Request No. 0196 requested Ameren Missouri to
4 identify the percentage of Ameren Corp's total assets that are considered non-utility assets.
5 In response to Dr. Won's data request, Mr. Sagel indicated that 1.19% of Ameren Corp's
6 total assets are considered to be "non-utility" assets.

7 **Q. Did Dr. Won consider this information supportive of using Ameren Missouri's per**
8 **books capital structure rather than considering Ameren Corp's consolidated capital**
9 **structure?**

10 A. Yes. Dr. Won considers this supportive of adopting Ameren Missouri's capital structure.
11 He testifies as follows in his direct testimony:

12 In addition, Ameren Corp.'s non-utility assets are around 1.2% of
13 its total assets. Hence, there are no significant concerns about the
14 financial relationship between Ameren Missouri's regulated utility
15 service and Ameren Corp's non-regulated business.[31]

16 Additionally, in discussing the four criteria in his rebuttal testimony, Dr. Won testifies as
17 follows after identifying that 1.19% of Ameren Corp's total assets are non-utility assets:

18 Therefore, there is no reason to use Ameren Corp's consolidated
19 capital structure for ratemaking capital structure of Ameren
20 Missouri according to the CRRA [Certified Rate of Return Analyst]
21 Guide upon which Staff relies.[32]

22 **Q. Is the fact that Ameren Corp is essentially a pure-play regulated utility supportive of**
23 **accepting Ameren Missouri's per books capital structure as fair and reasonable for**
24 **setting Ameren Missouri's ROR?**

25 A. No. Dr. Won testifies that he is not concerned about the financial relationship between
26 Ameren Missouri's regulated utility service and Ameren Corp' non-regulated business. I
27 am not concerned about this interrelationship either. In fact, if Ameren Corp had more

[31] Won Direct, p. 25, lines 3-5
[32] Won Rebuttal, p. 39, lines 9-11.

1 non-regulated operations, then it would be reasonable to expect Ameren Corp to have a
2 higher common equity ratio than Ameren Missouri.

3 For example, Algonquin Power & Utilities Corp ("APUC"), which is the ultimate parent
4 holding company of The Empire District Electric Company, is comprised of approximately
5 20-25% of non-regulated utility operations through its wholly-owned subsidiary
6 Algonquin Power Company. APUC targeted a higher common equity ratio for its non-
7 regulated subsidiary, Algonquin Power Company, versus a lower common equity ratio for
8 its regulated utility subsidiary, Liberty Utilities Company.[33] The higher common equity
9 ratio at Algonquin Power Company is not consistent with lower-risk profile of Liberty
10 Utility Company's regulated utilities, but this higher common equity is consolidated at
11 APUC. Using APUC's consolidated capital structure in such a situation may result in
12 ratepayers paying for a higher common equity ratio than that which is consistent with the
13 risk level of APUC's regulated utility subsidiary.

14 **Q. Would you summarize your main points in response to Dr. Won's and Mr. Sagel's**
15 **position to use Ameren Missouri's capital structure to set Ameren Missouri's ROR?**

16 A. Yes. Ameren Corp's actions speak louder than Ameren Missouri's testimony and data
17 request responses. Holding companies can provide benefits to utility subsidiaries through
18 certain economies of scale, but they can also be used to mislead as to the true market cost
19 of capital related to its subsidiaries. If Ameren Corp had its own source of income other
20 than from its regulated utilities, it might be plausible to claim that Ameren Corp issues debt
21 to assist its subsidiaries. This isn't the case. Ameren Corp is a parent company that relies
22 on the low-risk income of its subsidiaries to issue holding company debt rather than holding
23 company equity to invest in equity in its subsidiaries. Ameren Missouri can issue this debt
24 on its own and it would justly be captured in the ROR charged to Ameren Missouri's
25 ratepayers. Ameren Corp exists because of Ameren Missouri, not *vice versa*. If Ameren
26 Missouri was still directly accountable to third-party equity investors, its capital structure

[3333] Case No. ER-2021-0312, Todd Mooney Rebuttal, p. 13, l. 17 – p. 14, l. 7.

P

1 would be a function of market forces. Now it's a function of internal capital flows to meet
2 ratemaking targets.

3 ANN E. BULKLEY'S REBUTTAL TESTIMONY

4 *RETURN ON EQUITY*

5 **Q. Ms. Bulkley claims that you abandoned the results of your COE analysis for purposes**
6 **of your recommended allowed ROE range of 8.4% to 9.25%, point recommendation**
7 **of 9.25%.[34] Is she correct?**

8 A. No. My recommended authorized ROE of 9.25% takes into consideration many different
9 factors. A fundamental principle of shareholder value creation is for a company to invest
10 in projects that allow the company to at least earn its cost of capital. An allowed ROE of
11 9.25% allows for a margin of approximately 200 basis points over my estimate of Ameren
12 Missouri's COE in the range of 7.0% to 7.5%. I am aware investors have become
13 accustomed to regulators allowing utility companies returns that are higher than their cost
14 of capital. In fact, some investors, such as Evercore ISI, use investment models that assume
15 that regulators currently allow an ROE to COE spread of approximately 400 basis points
16 (9.75% ROE – 5.75% COE), but will eventually reduce the spread to a range of 225 to 285
17 basis points as either the COE increases, the allowed ROEs decrease or a combination of
18 both.[35]

19 The fact that the COE for Ameren Missouri is well below my recommended ROE,
20 establishes the reasonableness of my recommended authorized ROE. If the authorized
21 ROR is set above the cost of capital, Ameren Missouri can increase shareholder value
22 above the classic economically efficient amount simply by increasing rate base.
23 Regardless, my determination that the COE is slightly lower than at the time the
24 Commission authorized Ameren Missouri's current authorized ROE of 9.53% provides
25 support for reducing Ameren Missouri's authorized ROE to 9.25%. However, I also

[34] Bulkley Rebuttal, p. 4, lns. 18-20, and p. 56, lns. 4-13.
[35] Durgesh Chopra, et. al., "4Q Earnings Scorecard" Evercore ISI, March 5, 2023, p. 7.

1 understand from past Commission decisions that the Commission has set a zone of
2 reasonableness ("ZOR") that has generally been 100 basis points (1%) above and below
3 recent average authorized ROEs.

4 As reported by S&P Global Market Intelligence, the averaged electric utility authorized
5 ROE for 2022 was 9.54%. This average is slightly higher than the approximate 9.4%
6 average for the 9-months and 12-months periods-ending through September 30, 2022.
7 Based on the updated data through December 31, 2022, the low end of the Commission's
8 ZOR would be around 8.5%.

9 **Q. Ms. Bulkley asserts that you did not identify the proxy group you used to represent**
10 **the electric utility industry for purposes of analyzing changes in the industry's**
11 **valuation ratios over time.[36] Did you identify them?**

12 A. Yes, I identified the companies I used in footnote 9 on page 11 of my direct testimony.

13 **Q. Did this group include the companies you analyzed in Ameren Missouri's 2014 rate**
14 **case?**

15 A. Yes, with the exception of the four companies. Three companies, Great Plains Energy,
16 TECO Energy Inc. and Westar Energy Inc., are no longer publicly traded. I also removed
17 PNM Resources Inc. because it has been the subject of a pending merger with Avangrid
18 since October 2020.

19 **Q. Did you include any additional companies in the proxy group you used for the**
20 **valuation data you provided in your direct testimony?**

21 A. Yes. I included IDACORP and WEC Energy Group.

[36] Bulkley Rebuttal, p. 61, l. 5 – p. 62, l. 2.

P

1 **Q. Why?**

2 A. They were included in my proxy group in Ameren Missouri's 2012 rate case, Case No.
3 ER-2012-0166. Although these companies did not meet the criteria I applied in Ameren
4 Missouri's 2014 rate case,[37] they met the criteria I used in the 2012 rate case.[38]

5 **Q. To be absolutely clear, would you list all of the companies you used to represent the**
6 **electric utility industry for purposes of your analysis of valuation data you presented**
7 **in your direct testimony?**

8 A. Yes. They are: Alliant Energy Corporation, American Electric Power Company, CMS
9 Energy Corporation, DTE Energy Company, IDACORP, OGE Energy Corp, Pinnacle
10 West Capital Corporation, Portland General Electric Company, The Southern Company,
11 WEC Energy Group, and Xcel Energy Inc.

12 **Q. Although the above companies met your screening *criteria* at some point in the past,**
13 **have you expressed reservations about any of the companies' stock prices being**
14 **impacted by operations other their regulated electric utilities?**

15 A. Yes. As I testified in my direct testimony, I have reservations about including DTE Energy
16 Company and OGE Energy Corp for purposes of a time series analysis because their stock
17 prices, as demonstrated by periods of higher betas, have been impacted by exposure to
18 commodity risk through their midstream and energy marketing operations.

19 **Q. Ms. Bulkley suggests that because your multi-stage DCF COE estimates are below**
20 **any ROE authorized for a vertically-integrated electric utility over the last 40 years,**
21 **this illustrates that your COE estimate is unreasonable.[39] What is your response?**

22 A. Ms. Bulkley's position assumes that commission authorized ROEs reflect investors'
23 required returns for providing utilities' equity capital. I do not agree with Ms. Bulkley.
24 More importantly, investors do not agree with Ms. Bulkley. Based on my review of

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[37] *Id.,* Schedule 7.
[38] Case No. ER-2012-0166, Staff Cost of Service Report, Appendix 2, Schedule 7, July 6, 2012.
[39] Bulkley Rebuttal, p. 68, ll. 13-17.

1 practical investment analysis of utility stocks, if anything, my COE estimates are typically
2 higher than those used by investors to determine the fundamental value of a share of utility
3 stock.

4 **Q. Ms. Bulkley claims that your comparison of dividend yields for your representative**
5 **electric utility group since January 1, 2015, through current periods is biased because**
6 **you did not include dividend yields for the period of your analysis in Ameren**
7 **Missouri's 2014 rate case.[40] Do you agree that your analysis is biased?**

8 A. No. I simply selected January 1, 2015 because the Commission issued its order in April
9 2015 after reviewing and admitting evidence during the evidentiary hearing from February
10 23, 2015 through March 13, 2015. It should be noted that the Commission authorized
11 Evergy Metro an ROE of 9.5% based on market data from early 2015. As I will discuss
12 later, I sponsored ROR testimony on behalf of Staff at that time and also supervised other
13 Staff employees who sponsored ROR testimony (Shana Griffin and Zephania
14 Marevangepo). Between the time I sponsored testimony in Ameren Missouri's 2014 rate
15 case and the time Zephania Marevangepo sponsored testimony in Evergy Metro's 2014
16 rate case, the COE dropped another approximate 50 basis points, but because utility stock
17 prices had increased fairly dramatically in a short period of time, we decided it would not
18 be fair and reasonable to recommend a lower ROE for Evergy Metro as compared to
19 Ameren Missouri considering the proximity of the rate cases. Consequently, we
20 recommended a 9% to 9.5% ROE in both cases.

21 **Q. Can you expand the dates of the charts you included in your direct testimony to**
22 **include all of the 2014 calendar year?**

23 A. Yes, but please note I included information on the P/E ratios for this proxy group in my
24 direct testimony for the period since January 1, 2010. See pages 11 and 25 of my direct
25 testimony

26 The dividend yields for the expanded period are shown below:

[40] *Id.,* p. 66, l. 5 – p. 67, l. 3.

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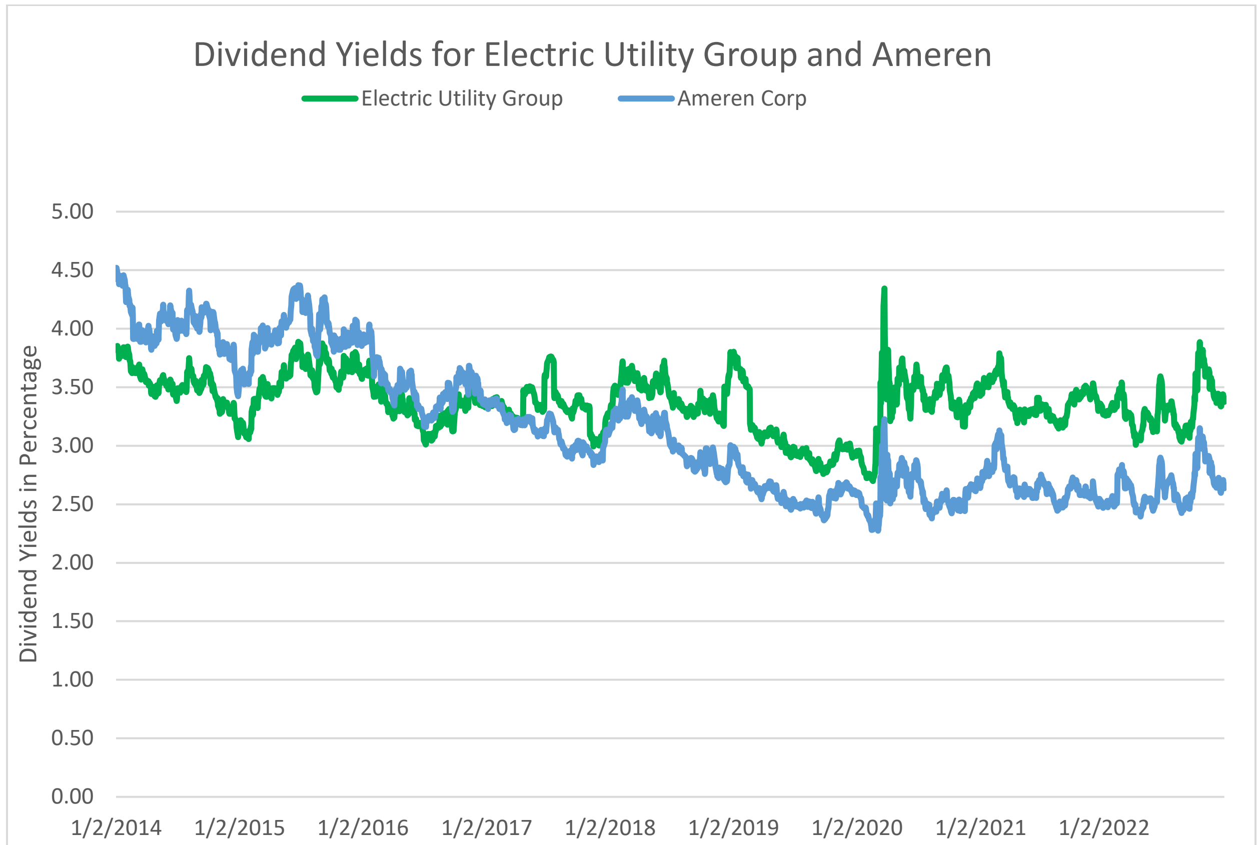
1 

2 **Q. What does the above chart of the electric utility group's dividend yields during the**
3 **time of Ameren Missouri's 2014 rate case and the current rate case demonstrate?**

4 A. That the electric utility group's dividend yields were consistently above 3.5% around the
5 time of Ameren Missouri's 2014 rate case compared to a few peaks of above 3.5% over
6 the last several years. The average daily electric utility dividend yield for the 2-year period
7 ending through December 31, 2015 was 3.55% compared to the 3.35% average daily
8 electric utility dividend yield for the 2-year period ending through March 7, 2023.
9 Consequently, evaluating a longer period of time during these two time periods establishes
10 the sustainability of lower electric utility dividend yields now compared to the general time
11 period of Ameren Missouri's 2014 rate case.

P

1 **Q. What does a comparison of Ameren Corp's dividend yields for the two periods imply?**

2 A. An even larger decline in Ameren Corp's cost of common equity than the electric utility
3 group. The average daily Ameren Corp dividend yield for the two-year period ending
4 through December 31, 2015 was 4.00% compared to Ameren Corp's 2.64% average daily
5 utility dividend yield for the two-year period ending through March 7, 2023.

6 **Q. Why did Ameren Corp's dividend yield decline over six times as much as the electric**
7 **utility group?**

8 A. As I explained in my direct testimony, Ameren Corp's business risk profile has declined
9 considerably due to investor-friendly legislation passed in both Missouri and Illinois.
10 Additionally, Ameren Corp's most investor friendly jurisdiction, the FERC, has already
11 awarded Ameren Corp $1.8 billion of Tranche 1 transmission projects under MISO's Long-
12 Range Transmission Plan with the possibility of an additional $700 million of competitive
13 greenfield projects.[41] Consequently, Ameren Corp's long-term growth profile, as well as
14 the certainty of its growth profile has improved considerably.

15 **Q. Is there a means by which to assess the attributions for the improvement in the**
16 **valuation levels of the electric utility industry and Ameren Corp's between the**
17 **current period and the period of Ameren Missouri's 2014 rate case?**

18 A. Yes. Investors typically compare a company's or industry's P/E ratio to its expected long-
19 term growth rate to evaluate whether a utility's P/E ratio is consistent with changes in long-
20 term growth (i.e. 3-5 year CAGR in EPS) expectations. Because the electric utility
21 industry's P/E ratio, and more specifically Ameren Corp's P/E ratio, has improved not only
22 due to a general decline in the cost of capital, but also expected increased investment
23 opportunities related to electrification and renewable energy investment initiatives, it is
24 important to consider such factors when attributing causation to changes in P/E ratios.

[41] Durgesh Chopra, et. al., "No Shortage of Opportunities," Evercore ISI, August 5, 2022.

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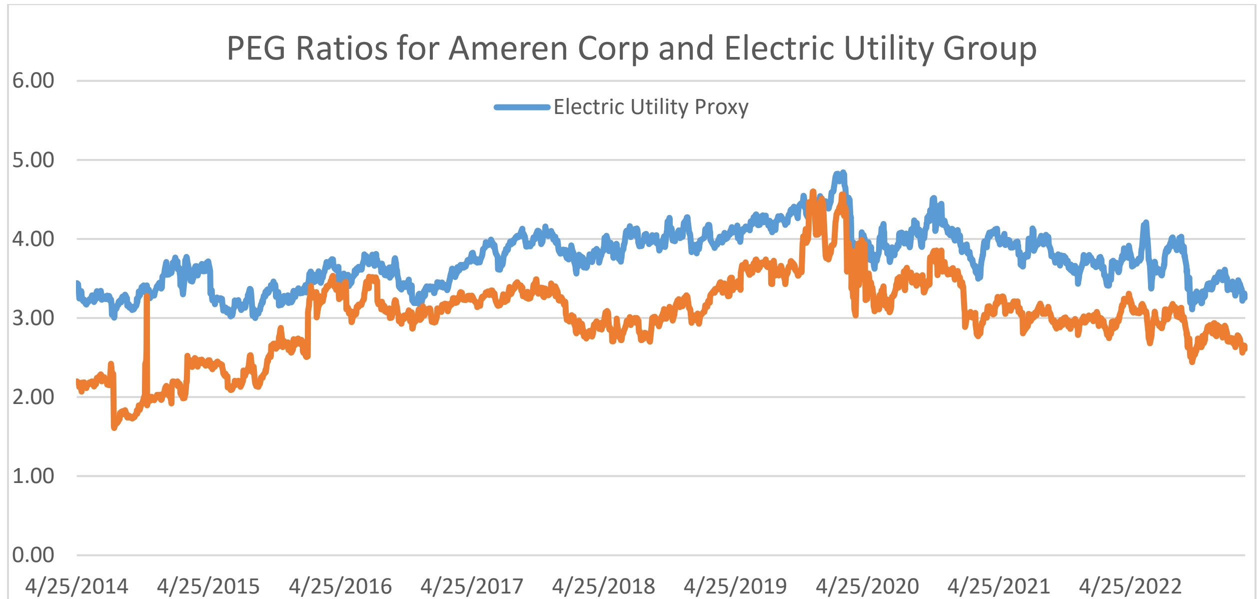
1 **Q. Can you provide a chart showing a time-series of the electric utility group's and**
2 **Ameren Corp's PEG ratios since early 2014?**

3 A. Yes. See the following:



4

5 **Q. Why did you not include PEG ratios for the period January 1, 2014, through April**
6 **25, 2014, as you did with P/E ratios?**

7 A. Because of the lack of consistently available long-term CAGR estimates in EPS before
8 April 25, 2014.

9 **Q. What do the PEG ratios imply about the electric utility industry's current COE**
10 **compared to the COE at the time of Ameren Missouri's 2014 rate case?**

11 A. It should be slightly lower.

12 **Q. Why?**

13 A. Because investors have recently been willing to pay a slightly higher P/E ratio as it relates
14 to long-term growth (around 3.25x to 3.5x) than they did in most of 2014 and 2015 (around
15 3.0x to 3.25x, except for a brief period in late 2014 and early 2015 when PEG ratios were
16 briefly around 3.5x).

P

1 **Q. Can you quantify the potential change in the COE based on analysis from the 2014**
2 **rate case compared to analysis in this case?**

3 A. Yes. As the ROR witness for Staff in Ameren Missouri's 2014 rate case, as well as the
4 supervisor of Staff's other ROR witnesses who sponsored testimony in the overlapping
5 2014 Empire and Evergy Metro rate cases, Case Nos. ER-2014-0351 and ER-2014-0370,
6 respectively, I can attest as to the methodology Staff relied upon to quantify Missouri's
7 electric utilities' COE at that time. Staff relied primarily on its multi-stage DCF analyses.
8 Staff filed its direct testimony in the Ameren Missouri 2014 rate case on December 5, 2014
9 and April 3, 2015 for the Evergy Metro rate case. Although Staff estimated that the
10 increases in utility stock prices over the four-month period between these two cases
11 demonstrated that the COE had declined by another 40 to 50 basis points (in addition to
12 the 25 to 75 basis points Staff had estimated the COE had declined since 2012), Staff
13 decided that due to the fact that the utility stock rally occurred within only three months
14 after Staff's analysis for the Ameren Missouri rate case, this short-term movement may not
15 be sustained. Therefore, Staff continued to recommend the same range of authorized ROEs
16 for Evergy Metro as it did for Ameren Missouri, which was in the range of 9% to 9.5%.

17 **Q. What was the implied COE for the electric utility industry based on your multi-stage**
18 **COE analysis in Ameren Missouri's 2014 rate case?**

19 A. In the range of approximately 7.5% to 7.65% using a 3% perpetual growth rate.[42]

20 **Q. Could you use the same companies from your 2014 COE analysis to estimate their**
21 **current COE?**

22 A. No. Three of the companies in the 2014 rate case are no longer independent, publicly-
23 traded entities (Great Plains Energy, TECO Energy Inc. and Westar Energy Inc.). A fourth
24 company, PNM Resources Inc. has been the subject of a potential acquisition by Avangrid
25 Inc. since October 21, 2020.[43]

[42] Case No. ER-2014-0258, Staff Cost of Service Report, Appendix 2, Schedule 12-1, December 5, 2014,
[43] S&P Global Market Intelligence.

1 **Q. Can you compare your 2014 COE estimate for these remaining companies to a**
2 **current COE estimate for the same companies?**

3 A. Yes. The 2014 COE estimate for the companies that can still be used today was 7.62%
4 (*see* Schedule DM-S-7). The current COE estimate using these same companies is 7.46%
5 (*see* Schedule DM-S-8).

6 **Q. What if you remove DTE Energy and OGE Energy from the proxy group due to the**
7 **concerns you raised earlier with including these companies?**

8 A. The COE estimate would be 7.76% in 2014 versus 7.43% now.

9 **Q. Ms. Bulkley testifies that your COE estimates for the electric utility industry have**
10 **increased since Ameren Missouri's 2019 rate case. Have they?**

11 A. Yes. I estimated the electric utility industry's COE was as low as the 5 percent range in
12 Ameren Missouri's 2019 rate case. My low COE estimate at the time was consistent with
13 the electric utility industry's all-time high P/E ratios of around 24x. Based on investors'
14 long-term expectations that authorized ROEs typically converge to around 225 basis points
15 higher than the COE, this would have justified me recommending an even lower authorized
16 ROE in the 2019 rate case, but I decided to make a measured recommendation in order to
17 attempt to convince the Commission that the then, extremely low COE, which had been
18 steadily declining for many years, supported at least some reduction to Ameren Missouri's
19 9.53% authorized ROE.

20 Because commissions have not lowered electric utility authorized ROEs consistent with
21 the significant decline in the COE, even with recent increases to the electric utility
22 industry's COE, there continues to be a considerable positive spread of authorized ROEs
23 over the COE. Based on my estimate of Ameren Missouri's current COE of approximately
24 7.25%, an authorized ROE of 9.25% allows a 200 basis point spread.

1 **Q. Did you provide corroborating evidence in Ameren Missouri's 2019 rate case that**
2 **demonstrated Ameren Corp's understanding of how low the COE was in 2019?**

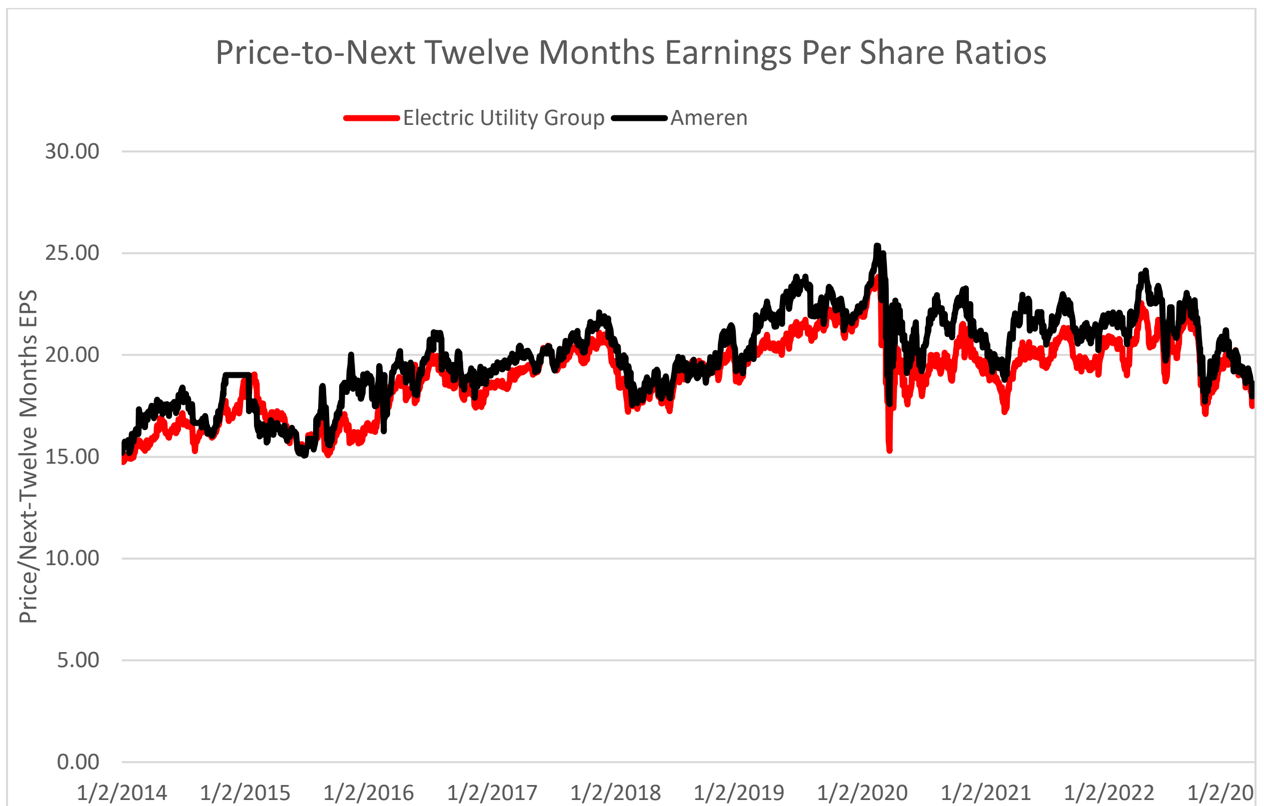
3 A. Yes. Schedules DM-D-11 (attached as Schedule DM-S-9), DM-D-12 and DM-D-16
4 attached to my direct testimony in Case No. ER-2019-0335 provided Ameren Corp's and
5 its investment bank's view of the favorability of the utility equity markets.

6 **Q. What was Ameren Corp's P/E ratio at the time it received advice from its investment**
7 **bank, Goldman Sachs?**

8 A. 22.3x, which compared to 20.3x for its peers. These compared to a 5-year average of 18.4x
9 for both Ameren Corp and its peers (see page 3 of Schedule DM-S-9).

10 **Q. How do these earlier P/E ratios compare to current P/E ratios?**

11 A. As with my comparison of Ameren Corp and the electric utility industry's dividend yields,
12 I will provide data for P/E ratios since January 1, 2014. The chart follows:



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1 As it relates to both Ameren Corp and the electric utility group, valuation levels have been
2 largely consistent with the levels Ameren Corp's investment banker had considered quite
3 favorable in 2019. Ameren Corp and the electric utility industry's valuation levels have
4 remained quite resilient even in spite of increases in long-term bond yields.

5 **Q. How do Ameren Corp's and the electric utility peer group's recent P/E ratios**
6 **compare to those in the 2014 and 2015 period?**

7 A. As can be seen in the above chart, both Ameren Corp and the electric utility group traded
8 in the range of 15x to 19x for most of 2014 and 2015. The electric utility group and Ameren
9 peaked at around 19x toward the end of 2014 and they contracted to around 15x again
10 around the middle of 2015. In contrast to the two-year period of 2014 and 2015, during
11 2021 and 2022, Ameren Corp's P/E ratio has frequently traded between 20x to 23x (even
12 during the rapid increase in long-term rates through the first nine months of 2022) only
13 hitting troughs of around 18x in mid-October of 2022 and early March 2023. Except for
14 recent months, the electric utility group traded a couple turns below Ameren Corp. As it
15 relates to both Ameren Corp and the electric utility group, valuation levels have been
16 largely consistent with the levels Ameren Corp's investment banker had considered quite
17 favorable in 2019. Ameren Corp's and the electric utility industry's valuation levels have
18 remained quite resilient despite increases in long-term bond yields. A common sense
19 interpretation of these valuation ratios supports not authoring Ameren Missouri a ROE any
20 higher than that which it was authorized in its 2014 rate case.

21 **Q. In Figure 8 of Ms. Bulkley's rebuttal testimony, she compares the results of your**
22 **various COE estimates for Ameren Missouri's last three rate cases. She testifies that**
23 **models other than your multi-stage DCF imply a significant increase in the COE since**
24 **2019. Do you agree?**

25 A. I agree that using these methods with standard inputs imply a higher COE than as recently
26 as 2020 and 2021, but the economy and capital markets have been anything but standard
27 since the onset of the Covid-19 pandemic. Contrary to Ms. Bulkley's assertion that my
28 recommended ROEs have been arbitrary without consideration of the cost of capital, I

1 recognized extremely low bond yields in 2020 and 2021 did not cause the utility industry's
2 COE to decrease in kind. In fact, as Ms. Bulkley notes, my COE estimates increased. As
3 is clear from Ms. Bulkley's Figure 8, I have largely dismissed my bond yield plus risk
4 premium ("BYPRP") tests of reasonableness since the Fed and US Treasury (as authorized
5 by the United States Congress) aggressively intervened in the economy and capital
6 markets. Logically, my multi-stage COE estimates were lowest in 2019 when utility P/E
7 levels were at their highest. Although my standard BYPRP indicated the electric utility
8 industry's COE was around 5.75% at the time of Ameren Missouri's 2021 rate case, I
9 dismissed this information because it was inconsistent with lower utility P/E ratios.
10 Similarly, although my standard BYPRP method implied that the electric utility industry's
11 COE is now over 225 basis points higher than when interest rates were lower, I recognized
12 that utility P/E ratios had not declined much despite increases in bond yields.

13 **Q. Ms. Bulkley cites a Bank of America ("BofA") equity research report to discredit your**
14 **use of a 2.5% to 3.5% terminal growth rate for purposes of your multi-stage dividend**
15 **discount model ("DDM").[44] What is your response?**

16 A. She misinterpreted BofA's use of long-term CAGR in EPS. The valuation analysis
17 performed by BofA is a relative P/E analysis for purposes of estimating price targets. It is
18 not an absolute valuation analysis which discounts fundamental financial metrics, such as
19 dividends. BofA's P/E analysis is sometimes referred to as an "agnostic" analysis because
20 it accepts a current industry and/or peer average P/E ratio as being a fair market price for
21 an average company in the industry. The analyst will then assign P/E premiums or
22 discounts based on favorable or unfavorable characteristics of the company. BofA may
23 assign a company, such as Ameren Corp, a premium because it has a higher than average
24 expected long-term CAGR in EPS as compared to the average for the industry. BofA *is*
25 *not* using the long-term CAGR as a perpetual growth rate for an absolute analysis such as
26 a dividend discount model ("DDM"). I have provided multiple examples of much more
27 reasonable perpetual growth rates used in a DCF analyses. Actually, in Ameren Missouri's
28 2021 rate case, I cited a DCF analysis ** ______________________________

[44] Bulkley Rebuttal, p. 72, line 1 through p. 74, line 5.

P

1 ____
2 ________________________ **[45]

3 **Q. How does BofA value Ameren Corp?**

4 A. It assigns a 2x P/E premium to Ameren Missouri's and Ameren Illinois's EPS and a 4x
5 premium to ATXI's EPS.[46]

6 **Q. Ms. Bulkley claims that you should have used a constant-growth DCF using equity**
7 **analysts' long-term CAGR in EPS as the constant growth rate.[47] What is your**
8 **response?**

9 A. Ms. Bulkley testifies that applying the constant-growth DCF using equity analysts'
10 projected long-term CAGR in EPS is consistent with the views of equity analysts.
11 However, in the concurrent MAWC rate case, Case No. WR-2022-0303, I requested Ms.
12 Bulkley to provide a practical example of equity analysts valuing stocks in this fashion.
13 She could not provide an example. She indicated her testimony was based on her twenty
14 years of experience reviewing equity analyst earnings per share ("EPS") growth rate
15 forecasts (see Schedule DM-S-10). She apparently believes reviewing EPS forecasts, and
16 not the equity analysts' more detailed analysis provided in their reports, as sufficient to
17 support her testimony.

18 **Q. Ms. Bulkley claims that your 6% market risk premium is unreasonable. How do you**
19 **respond?**

20 A. ** ____
21 ____
22 ___________________________________ **[48]

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[45] Case No. ER-2021-0240, Murray Direct, p. 22, lines 1-6.
[46] Julien Dumoulin-Smith, et. al., "Ameren Corporation – 2023 EPS preview: Intact outlook amid elevated regulatory hurdles in near term," Bank of America, January 6, 2023
[47] Bulkley Rebuttal, p. 76, lines 3-17.
[48] Case No. ER-2019-0335, Murray Direct, Schedule DM-D-16.

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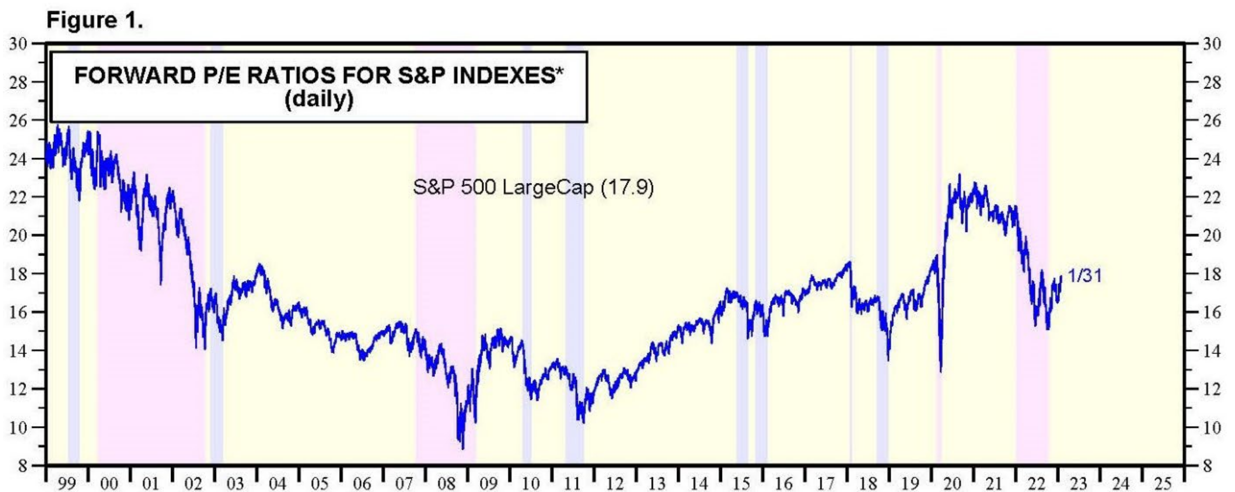
Q. Ms. Bulkley shows annual stock market returns for the 13-year period 2009 to 2021 to support her high market risk premium estimates.[49] If you used the 13-year period ending in 2008, what would this information imply about market risk premium estimates starting in 2009 when the S&P 500 had just declined by 37% in 2008?

A. The arithmetic average annual S&P 500 market returns for the period 1996 to 2008 was 7.05%. The arithmetic average annual long-term United States Treasury ("UST") bond returns over this same period was 8.98%. Based on Ms. Bulkley's logic of using a recent 13-year total return to estimate a market risk premium, this would imply that investors' market risk premium was a negative 1.93% over UST bonds at the beginning of 2009.

Q. What do you conclude?

A. These arbitrary periods should not be used to justify an implied market risk premium. It is widely understood that during periods when the S&P 500 is trading at high valuation levels, the required returns going forward are lower, and when the S&P 500 is trading at lower levels, the required returns going forward are higher. See the following chart which shows the valuation levels of the S&P 500 over the last couple of decades:



[49] *Id.*, p. 80, lines 1-2.

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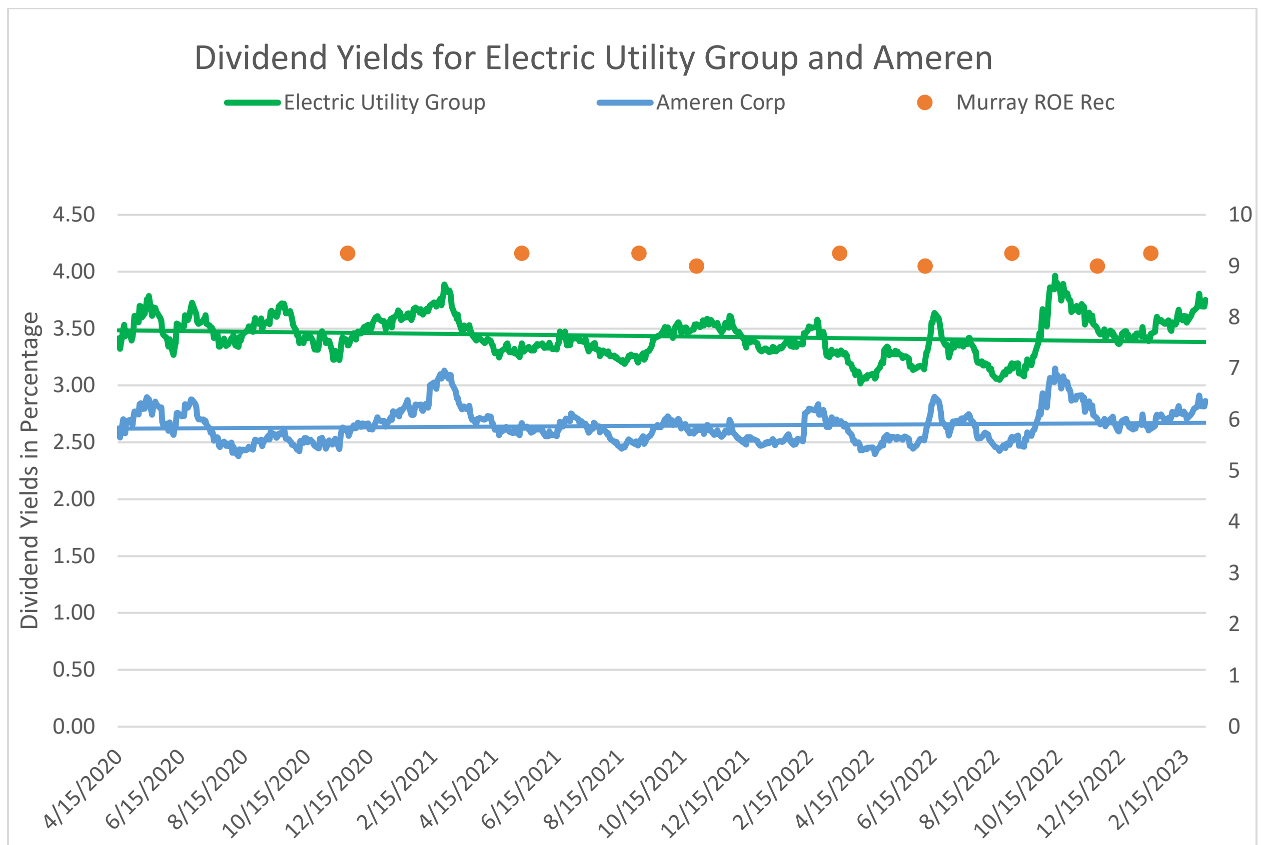
1 **Q. Ms. Bulkley provides a chart on page 61 of her rebuttal testimony where she compares**
2 **your recommended ROEs to inflation and 30-year Treasury yields. What is your**
3 **response?**

4 A. A more appropriate comparison is to plot my recommendations against my electric utility
5 industry group's dividend yields and Ameren Corp's dividend yields subsequent to the
6 onset of Covid-19. That comparison follows:



7

8 Before Covid-19, there was a clear downward trend line for the utility group's dividend
9 yields and, consequently, an upward trend line for P/E ratios. However, there have been
10 no clear trends since the onset of Covid-19 despite increases in inflation and bond yields.
11 Therefore, my consistent ROE recommendation over the last several years are logical.
12 Although Ms. Bulkley did not identify such, my recent 9% recommended ROE was for
13 MAWC because market valuation data clearly showed that water utilities have a lower
14 COE than electric and gas utilities. I started to recommend a 9.25% ROE for gas utilities

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1 as recently as Ameren Missouri's last gas rate case because LDC's had been trading at a
2 discount to the other utility subsectors. Finally, I decided to increase my recommended
3 ROE for Ameren Missouri because of the decline in electric utility valuations in the fourth
4 quarter of 2022.

5 **Q. In Figure 1 of her rebuttal testimony, Ms. Bulkley compares current 30-year UST**
6 **bond yields and authorized ROEs to those around the time of the financial crisis from**
7 **2007 to 2009. Are these two periods similar as it relates to the valuation levels of**
8 **utility stocks?**

9 A. No. I sponsored testimony in Ameren Missouri's 2010 rate case, Case No. ER-2010-0036.
10 During my discovery in that rate case, I reviewed equity research reports published on the
11 electric utility industry. I discovered that when stocks, including utility stocks, dropped to
12 their nadir in March 2009, Goldman Sachs estimated the electric utility industry's COE
13 was 11.3%.[50] In March 2008 and September 2009, when electric utility stocks were trading
14 in a range consistent with their long-term averages, at the time, of around 12.5x on two-
15 year forward fiscal year EPS estimates (FY2), Goldman Sachs estimated the electric utility
16 industry's COE was around 8.9%.

17 **Q. Did Goldman Sachs express concern utilities may only earn a ROR similar to their**
18 **cost of capital when it estimated electric utilities' COE was around 11.3% on March**
19 **10, 2009, the day after the nadir for the S&P 500?**

20 A. Yes. Goldman Sachs indicated the following in a March 10, 2009 equity research report:

21 **If implied costs of equity remain high or authorized RoEs do not**
22 **increase, companies will likely decrease longer-term capital spending**
23 **and rate base growth – reducing our 4-5 year EPS growth outlook**
24 **below current levels.** Our implied DDM [dividend discount model]
25 analysis shows that the implied cost of equity has increased by
26 approximately 27% since March 2008 to levels near 11.3% - above where
27 regulators recently set authorized returns on equity. Authorized returns are
28 key given the increased costs of equity and debt ñ if authorized rates of
29 return set by regulators do not increase, many companies will face
30 challenges of earning a WACC-like return on capital investment, driving

[50] Case No. ER-2010-0036, Murray Rebuttal Testimony, p. 25, line 3 – p. 28, line 20.

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> them to reevaluate and potentially reduce longer-term discretionary spending where possible. Alternatively, if the cost of equity declines as stock prices increase or bond yields decrease, companies will face less economic pressure to reduce capital spending. (emphasis in original).[51]

Q. What was your COE estimate in Ameren Missouri's 2010 rate case?

A. 9% to 9.7% based on my analysis of market data during the Fall of 2009. Therefore, I was slightly above Goldman Sachs' estimates.

Q. How do Ms. Bulkley's COE estimates now compare to Goldman Sachs estimate when utility stock P/E ratios plummeted to single digits in March of 2009?

A. Ms. Bulkley suggests that the electric utility industry's current COE could be even higher than 11.3%. Her analysis of the electric utility industry suggests the COE could be as high as 11.8%.[52]

Q. Can you provide a chart showing overall utility P/E ratios since 2008?

A. Yes. However, I should note that it becomes more difficult to perform a time series analysis of groups of utility companies over longer periods of time. Many companies that are now pure-play regulated utilities, such as Ameren Corp, have gone through transformations over the last 10 to 15 years. Ameren Corp had significant risk related to its merchant generation operations it owned through Ameren Generation Company until Ameren Corp divested these operations in 2013. Similar situations have occurred with other companies. It is for these reasons that I used proxy companies from Ameren Missouri's 2012 and 2014 rate cases to represent changes in regulated electric utilities' valuation ratios over time. Because these companies passed my *criteria* in 2012 and 2014, I have confidence that at least for market valuation information starting in 2012, this group provides a reasonable representation of investors' views of regulated electric utilities. With that *caveat*, please see the below chart showing electric utility P/E ratios since January 1, 2008:

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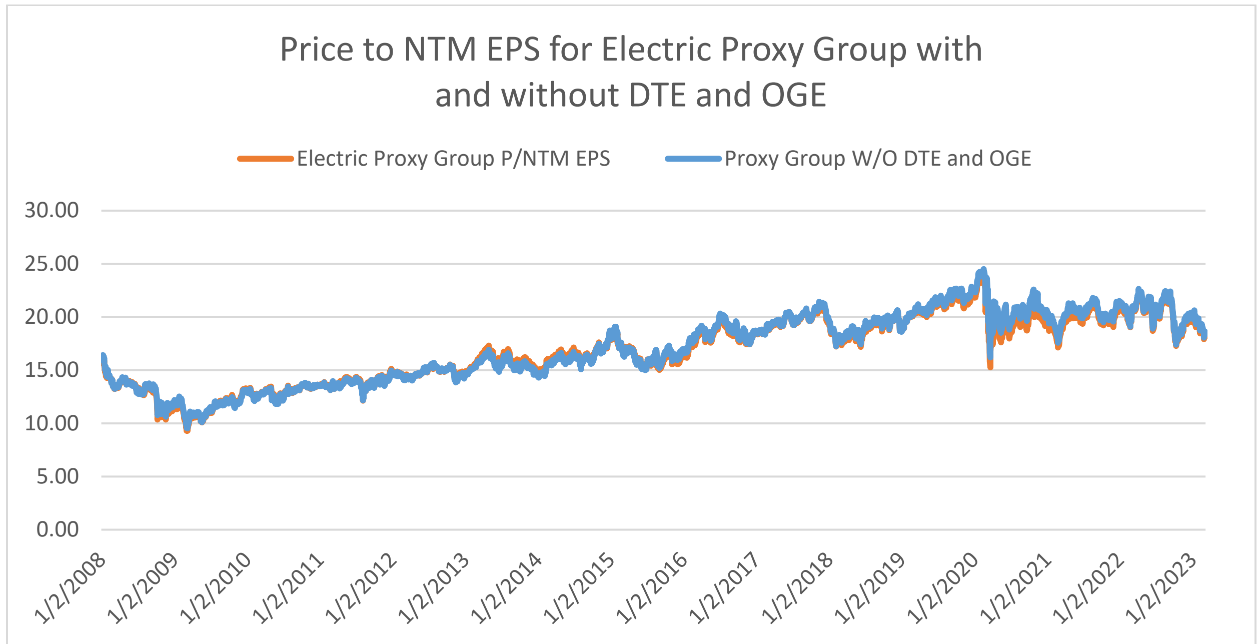
[51] Michael Lapides, et. al., "Reiterate Neutral Coverage View; POR replaces NVE as CL Buy," Goldman Sachs, March 10, 2009.
[52] Bulkley Direct, Figure 2, p. 13.



As is evident from the above graph, electric utility P/E ratios were at their lowest level on March 9, 2009, at about a 9.5x P/E ratio. Even with the recent contraction in electric utility P/E ratios, they are still about twice the level they were when Goldman Sachs estimated electric utilities COE was 11.3%. For Ms. Bulkley to suggest authorized ROEs should be set similar to average levels at that time shows a complete disregard for the context of current utility stock valuation levels. While electric utility companies' sustainable long-term growth rates have likely improved due to electrification and carbon dioxide emission reduction initiatives, electric utilities' long-term CAGR in EPS are still on average close to 6%, which is similar to the long-term CAGR in EPS for electric utilities in 2010.[53] Consequently, the most plausible attribution for electric utility higher P/E ratios is a lower cost of common equity. Contrary to Ms. Bulkley's position that DCF methodologies should be dismissed in the current market environment, they should be weighed heavily considering the fact that this is the only methodology that directly analyzes utility stock prices compared to their fundamentals.

My cost of common equity estimates of a little over 9% in 2010 compared to my current cost of common equity estimates of around 7% are quite rational when viewed in the

[53] Case No. ER-2010-0036, Staff Cost of Service Report, December 18, 2009, Appendix 2, Schedule 12.

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1 context demonstrated by the above chart. As I explained previously, investors are
2 accustomed to commissions authorizing ROEs higher than the COE. Because this
3 paradigm became even more obvious during the utility industry's extended period of low
4 cost of capital, my primary objective has been to convince the Commission that it is
5 reasonable to reduce authorized ROEs in the range of 25 to 50 basis points.

6 **Q. Ms. Bulkley cites Moody's opinion that authorized ROEs could increase as a result of**
7 **recent increases in interest rates.[54] Are you aware of investor commentary that**
8 **expresses concerns that ROEs may actually be lowered due to utility rate pressures**
9 **related to inflation and potential recession?**

10 A. Yes. Investors have long recognized that commissions had not reduced ROEs as much as
11 reductions in the cost of capital may justify. Many equity analysts characterized this lag
12 in reducing ROEs as "stickiness." For example, Mizuho Securities USA LLC recently
13 stated the following about recent increases in interest rates:

> 14 ROE "stickiness" should most likely prevail, even though utilities are filing
> 15 rate cases asking for higher ROEs. We believe regulators didn't
> 16 significantly reduce ROEs while rates were declining and thus believe they
> 17 will be reluctant to raise ROEs while rates are increasing.[55]

18 Because commissions did not reduce ROEs even though lower costs equity justified doing
19 so, investors expect potential "stickiness" for potential increases in authorized ROEs. This
20 is logical considering the fact that any recent increases in the COE are simply lowering the
21 margin of authorized ROEs over the COE.

22 **<u>SEOUNG JOUN WON'S REBUTTAL TESTIMONY</u>**

23 **Q. What are Dr. Won's primary criticisms of your ROE recommendation?**

24 A. Similar to Ms. Bulkley, Dr. Won asserts that because the COE has increased since the
25 Commission authorized Empire a 9.25% ROE in Case No. ER-2019-0374, this justifies

[54] Bulkley Rebuttal, p. 8, lines 1-5.
[55] Anthony Crowdell, et. al., "Takeaways from Mizuho Utilities Summit," Mizuho Securities USA LLC, November 29, 2022, p. 1.

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1 Ameren Missouri being authorized a higher ROE. This is literally too short-sighted. While
2 utility valuations are more compressed than they were shortly before the pandemic, they
3 are still more highly valued than the first time the Commission deemed 9.5% ROEs
4 reasonable in 2015. As is evident from my divergent COE estimates using various different
5 methodologies, it is very important to determine if the COE estimates are consistent with
6 market indicators, such as P/E ratios. At least the direction of my multi-stage DCF COE
7 estimates are consistently supported by utility stock valuation levels. This has not been
8 true for my CAPM and BYPRP estimates, which don't directly consider utility stock prices
9 and underlying fundamentals.

10 **Q. Did Dr. Won request you to elaborate further on your COE estimate in this case?**

11 A. Yes. Please see my attached response to Dr. Won's Data Request No. 0469 (Schedule
12 DM-S-11). I will not repeat the answer, but I explained that considering utility stock
13 valuations had not declined as long-term interest rates increased in 2022, I placed almost
14 no weight on interest-rate sensitive COE methods.

15 **Q. Does Dr. Won question the relevance of analyzing P/E ratios in estimating the COE**
16 **and setting authorized ROEs?**

17 A. Yes. Dr. Won testifies as to his views on page 31, line 15, through page 32, line 4 of his
18 rebuttal testimony. Dr. Won also requested an explanation from me as to the relevance of
19 P/E ratios in estimating the COE. I provided a response to Dr. Won's DR No. 472 as to
20 the relevance of P/E ratios in evaluating the COE estimates *(see* Schedule DM-S-12). In a
21 nutshell, a higher P/E ratio is driven by two primary factors, discount rates (*i.e.*, the COE)
22 and expected growth rates. Utilities have long been viewed as a steady-growth, predictable
23 industry. Therefore, P/E ratios for utilities are not likely to change much due to changes
24 in growth expectations. In fact, I showed this in the PEG charts I provided earlier in
25 response to Ms. Bulkley's testimony. Consequently, the main factor usually influencing
26 utility P/E ratios are changes in the COE. Consequently, while I agree with Dr. Won that
27 P/E ratios are not directly used to estimate the COE, they are very instrumental in assessing
28 whether COE estimates are consistent with underlying fundamentals. Based on recent

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market conditions and consideration of P/E ratios, COE methods using bond yields are not providing logical results.

Q. Did you make any other responses to Dr. Won's DRs that you believe would assist the Commission for deciding ROR in this case?

A. Yes. I am attaching my responses to Dr. Won's DR Nos. 478 and 555 as Schedules DM-S-13 and DM-S-14, respectively, to my testimony.

SUMMARY AND CONCLUSIONS

Q. Would you summarize your points in this surrebuttal testimony?

A. Yes. This is not the first time Ameren Corp has tried to preserve a higher equity ratio at its regulated subsidiary after significant legislative strategies allowed for more favorable ratemaking. It is also not unique to compare the parent company's financing structure to that of its subsidiaries when evaluating a fair and reasonable ratemaking capital structure. The Commission need look no further than its two neighboring states, Illinois and Kansas, for some guidance on this issue. Illinois went as far as codifying a 50% ratemaking equity ratio into law, but not until after the ICC Staff stood its ground in arguing for a more reasonable common equity ratio than that shown in Ameren Illinois' "independently" managed capital structure. Kansas required a cap on equity ratios for purposes of approving the merger of equals transaction between Great Plains Energy and Westar Energy, with the cap being adjusted downward if the new holding company used too much leverage. As it relates to Missouri's ability to limit excessive common equity ratios, it is up to this Commission to do so in context of this rate case. Doing so will not cause a decline in Ameren Missouri's credit quality unless Ameren Corp refuses to offset this financial risk by reducing the amount of holding company debt in its capital structure.

The Commission should authorize Ameren Missouri an ROE of 9.25%. While utility P/E ratios have declined slightly in recent months, this only occurred after a sustained period of P/E ratios that in 2015 had not been achieved. Authorized ROEs have proven to lag changes in the COE. This may be for good reason. A trend is defined by the analyst.

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1 While Dr. Won and Ms. Bulkley define a trend in COE increases as since late 2019, early
2 2020 until now, I still consider the longer-term trend since 2015 or even since 2010 since
3 Ms. Bulkley compares current market conditions to that period. Based on the longer-term
4 context, authorized ROEs for utilities should not be raised.

5 **Q. Does this conclude your testimony?**

6 A. Yes.

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BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Union Electric Company	)	
d/b/a Ameren Missouri's Tariffs to Adjust	)	Case No. ER-2022-0337
Its Revenues for Electric Service	)	

AFFIDAVIT OF DAVID MURRAY

STATE OF MISSOURI)
) **ss**
COUNTY OF COLE)

David Murray, of lawful age and being first duly sworn, deposes and states:

1. My name is David Murray. I am a Utility Regulatory Manager for the Office of the Public Counsel.

2. Attached hereto and made a part hereof for all purposes is my surrebuttal testimony.

3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.

David Murray
Utility Regulatory Manager

Subscribed and sworn to me this 8th day of March 2023.

TIFFANY HILDEBRAND
My Commission Expires
August 8, 2023
Cole County
Commission #15637121

Tiffany Hildebrand
Notary Public

My Commission expires August 8, 2023.