Exhibit No. 2

Ameren – Exhibit 2
Kelly Hasenfratz
Rebuttal Testimony
File No. ER-2022-0337

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Issue(s):	
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MISSOURI PUBLIC SERVICE COMMISSION

FILE NO. ER-2022-0337

REBUTTAL TESTIMONY

OF

KELLY HASENFRATZ

ON

BEHALF OF

UNION ELECTRIC COMPANY

D/B/A AMEREN MISSOURI

St. Louis, Missouri
February 15, 2023

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REBUTTAL TESTIMONY

OF

KELLY HASENFRATZ

FILE NO. ER-2022-0337

I. INTRODUCTION

Q. Please state your name and business address.

A. Kelly Hasenfratz, Union Electric Company d/b/a Ameren Missouri ("Ameren Missouri" or "Company"), One Ameren Plaza, 1901 Chouteau Avenue, St. Louis, Missouri 63103.

Q. By whom are you employed and in what capacity?

A. I am employed by Ameren Services Company ("AMS") as Director, Compensation & Performance.

Q. Please describe your educational background and employment experience.

A. I was awarded a Bachelor of Science in Business Administration in 1985 from the University of Missouri – Columbia. I have over 30 years of experience with Ameren in increasingly responsible roles – more than 25 of which were focused on total rewards and human resources-related activities. I have been in my current role since December 2015. In my current role, I am responsible for overseeing the strategy, design and delivery of broad-based compensation and executive compensation programs and processes for Ameren and its subsidiary companies. This includes base pay infrastructure, merit, short- and long-term incentive programs, paid time off and recognition programs.

II. PURPOSE OF TESTIMONY

Q. What is the purpose of your rebuttal testimony in this proceeding?

A. I am responding to the Missouri Public Service Commission Staff witness Matthew Young, regarding Staff's positions on employee compensation matters. Specifically, I will address how Restricted Stock Units ("RSUs") differ from other forms of stock-based compensation agreements in the Company's Long-Term Incentive Plan ("LTIP"). RSUs reflect competitive and reasonable compensation for employees that provide tangible benefits to our customers and should therefore be reflected in the revenue requirement used to set rates in this case. I will also address the cost associated with the Exceptional Performance Bonus Program and Severance Plan.

III. RESTRICTED SHARE UNITS

Q. Please explain Staff's recommendation related to the cost of RSU awards?

A. Staff recommends that the entire cost of the Company's LTIP, comprised of both RSUs and Performance Share Units ("PSUs"), be assigned to shareholders, rather than reflecting the cost of the RSUs in the revenue requirement used to set Ameren Missouri's electric rates. Staff makes no distinction between PSUs, for which the Company is not seeking recovery, and RSUs. In general, Staff's rationale for disallowing recovery of RSUs is the same as the Company's rationale for not seeking recovery of its PSUs, despite RSUs having meaningful differences from the Company's PSUs. Staff claims that "Historically, the Commission has consistently assigned the portion of incentive compensation expense that is tied to shareholder benefit to the utility's shareholders." Additionally, Staff references the Company's response to Data Request No. 22, where the Company provided the intent of the entire LTIP plan.

Q. Are RSUs awarded based on goals that relate to shareholder benefits?

A. No.

Q. What are RSUs and how do they differ from other forms of stock-based compensation such as the Company's PSUs?

A. RSUs represent the right to receive stock depending solely on an employee's continued employment with Ameren through a defined vesting period. As a starting point, RSUs and PSUs have fundamental differences; otherwise there would be no logical rationale to grant awards with different characteristics (i.e., all could be either PSUs or RSUs). Unlike PSUs tied to a financial performance measure (like Relative Total Shareholder Return) which primarily benefit shareholders; RSUs represent the right to receive stock depending solely on an employee's continued employment with Ameren Missouri through a defined vesting period, and thus are not based on the Company's financial performance. RSUs are awarded to encourage retention and longevity with Ameren and have no value to the employees unless the employee remained employed for the defined vesting period. A stable workforce benefits Ameren Missouri's customers with retained talent and the avoided costs of employee turnover, which are considerable. Consequently, RSUs provide meaningful benefits to customers. Moreover, with continued employment being the <u>only</u> requirement to receive the RSUs, this award contains a service condition per United States Generally Accepted Accounting Principles ("US GAAP"). RSUs will always pay out at 100% of the targeted share level, so long as the employee meets the service criteria. Again, this distinguishes RSUs from PSUs that pay out based solely on financial performance, or other pre-established operational performance measures. PSUs and RSUs complement each other as they align employees with the interest of different stakeholders – for PSUs shareholders, and for RSUs, customers.

By contrast, PSUs represent the right to receive stock if, at the end of a defined performance period Ameren has met certain performance targets regarding relative total shareholder return ("TSR") as compared to a pre-determined group of peer utilities (or other operational or financial metrics). Since PSUs are based on the operations or activities of the Company, this award contains a performance condition. PSUs could pay out at 0% or 200% of target (or somewhere in between) based on the performance of the Company compared to the defined performance parameters. The Company's PSU awards in this case contain a performance condition based on relative TSR compared to peer utilities. This comparison to a peer group normalizes for the impact of overall market forces on the stock price (as best as it can) and evaluates the Company's performance relative to other peers in the industry. The performance condition of the PSUs applicable to this case is tied solely to relative total shareholder return and clearly aligns with shareholders' interests. I offer this distinction to show that other respected regulatory bodies (i.e., The Financial Accounting Standards Board) meaningfully differentiate between the Company's PSUs and RSUs.

Q. How do RSUs differ from any non-stock-based compensation?

A. RSUs are a component of the total compensation package offered to the Ameren Leadership Team ("ALT"), which is defined as management employees from the Director level up to the Officer level, as part of the LTIP. Base pay and short-term incentive compensation, while necessary components of Ameren's total compensation package, do not require the employee to remain employed for 36 months before receiving payment. So, while all compensation incentivizes employment itself, RSUs specifically incentivize continued employment for an established duration.

Q. Why were PSUs reduced and RSUs added to the LTIP, and how does this change benefit customers?

A. PSUs were reduced and RSUs were added to the LTIP in 2018 after completing a comprehensive study of peer company LTI compensation market practices. Regular studies of market practices are performed to ensure aspects of the Company's total rewards remain attractive to current and future employees. This study found that Ameren's plan differed from market practice in that our plan was 100% performance based and was trying to achieve both performance and retention goals in one plan. Peer companies' plans were 70% – 75% performance based, with two-thirds of the peer companies including a time-based restricted stock to aid in retention. On that basis, we took the same step that had already been taken by two-thirds of our peers and added RSUs to create a greater incentive for our employees to continue their employment with us. The most recent study completed in 2022 showed that 85% of peer companies grant time-based restricted stock units as part of the annual LTI grant, and consistent with Ameren's LTIP, time-based awards make up approximately 30% of the award (median of companies in study).

RSUs are a common component of total compensation for Director and Officer-level roles at peer utilities. They encourage and reward longevity, which benefits customers not only by providing an experienced leadership team, which will provide more effective and efficient management, leading to lower overall costs and better service, but also by avoiding the productivity loss and replacement costs associated with turnover. RSUs motivate employees to stay and remain dedicated to serving our customers, rather than look for new employment.

Having RSUs as part of the Company's total compensation plan also serves to attract and retain a sufficient, qualified, and motivated work force. There are a number of benefits that inure to customers from a tenured and experienced workforce. Encouraging the retention of tenured employees' benefits customers by having leaders who are experienced in overseeing utility services generally, but who are also familiar with the uniqueness of Ameren Missouri's service area. The process of having to recruit and replace tenured employees with newer and/or less experienced employees, of course, requires training and a learning curve to ensure optimal processes for the benefit of our customers. There are also costs associated with recruiting and hiring replacements, and those costs tend to be higher at the ALT level. Given the extremely tight labor markets we are seeing in the U.S. generally, and which Ameren also sees, attracting and retaining employees is more important than ever.

Q. How does a stable workforce benefit customers?

A. Significant personnel turnover should be avoided from a pure operations standpoint, for obvious reasons. A stable workforce avoids the costs of employee turnover. This in turn keeps the labor costs that are ultimately reflected in the revenue requirement down. Clearly, the Company's RSU expense is prudent, reasonable and operates in a way to benefit the Company's customers. Specifically, Josh Bersin, a respected global industry analyst with Bersin by Deloitte, suggests it can cost 2 – 3x first year salary to replace an employee, and he points out that in a tight labor market, the cost gets much higher.[1] For

[1] *See,* Josh Bersin, "*What To Expect In A Red Hot Job Market? Five Things To Consider.*" Published March 9, 2021, Updated March 11, 2021

example, replacement costs include recruiting costs, onboarding, cost/time for training, lost productivity and ramp-up time. Employees get more productive the longer they are at a company, having learned the systems, the products and how to work together with their teams – all of which benefit customers.

Q. Have you quantified any avoided cost of employee turnover?

A. Yes. While the Company does not track all tangible and intangible costs of ALT employee turnover, the most tangible data we have is related to the cost to recruit and onboard an experienced leader at the Officer level. In most cases, these individuals will have similar compensation packages to what Ameren offers, with vesting periods designed to promote retention. It is frequently necessary for companies to offer sign-on bonuses as part of the offer of employment to attract experienced leaders. At the Officer level, this cost alone has averaged approximately 1.8x base pay, based on three senior-level officer hires at Ameren since 2016. This value does not include other costs, such as relocation, recruitment costs when using an external search firm, lost productivity and training. Ameren's history with hiring senior level Officers is in line with Josh Bersin's estimate of 2 – 3x first year salary to replace someone, as previously referenced. By avoiding ALT turnover costs, the Company can keep the labor costs that are ultimately reflected in the revenue requirement down. Cleary, the Company's RSU expense is prudent, reasonable and operates in a way to benefit the Company's customers.

Q. Is voluntary turnover at the ALT level low in Ameren Missouri?

A. Since 2018, Ameren Missouri has only had two voluntary terminations at the ALT level, for reasons other than retirement – one in 2021 and one in 2022. This equates to a voluntary attrition rate of 1.4% for both years, compared to 2.1% voluntary attrition in 2021 and 3.9% voluntary attrition in 2022 for all other Ameren Missouri employees.

Q. Staff applied the same Commission guidance from Case Nos. EC-87-114 and ER-2006-0314 to the LTIP in this case and Staff argues that the primary incentive for an employee receiving the RSUs portion of the LTIP is to increase the Ameren share price.[2] How do you respond?

A. I completely disagree. The primary purpose of the RSU is to incent an employee to continue their employment through the payment date. The basis that underlies US GAAP and the determination of the Company's RSUs containing only a service condition, further supports the Company's conclusion that the primary incentive is continued employment. Acceptance of Staff's view would be an outright indication that the decisions called for under US GAAP are flawed and incorrect. The amount of RSUs awarded to an employee is solely based on retaining employment for the defined period, regardless of whether the stock appreciates or depreciates in value. Unlike the Company's PSUs that are based on TSR, which I described earlier; it is not feasible to believe an employee can overpower overall market forces to increase their RSU awards. Any fluctuation in valuation of the Company's stock price during the vesting period is a risk borne by the employee and, secondary or indirect, as compared to the primary incentive of continued employment.

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[2] File No. ER-2022-0337, Direct Testimony of Matthew R. Young, at 11, ll. 11-20, January 10,2023.

Q. Is there an alternative to Staff's recommended disallowance if the Commission desires to allocate these costs between shareholders and customers?

A. Yes. If the Commission is truly concerned with the mere presence of stock in the plan or share price fluctuations during the term of the award, an alternative that at least partially recognizes the benefits customers receive from RSUs would be to allow recovery of the cost of its RSUs at the grant date of the award. This is the value of the award as if it were cash on the date the award is granted. If the Commission were to order it so, in this case, the Company would include $2,753,821 (as compared to the Company's position of $3,620,163) of long-term incentive compensation in its revenue requirement used to set rates in this case.

Q. Staff cites the Company's policy, presumably as evidence RSUs primarily benefit shareholders. How do you respond?

A. Staff's reference to the Company's policy is a description of the goals of the LTIP plan, as a whole. For the sake of clarity, the primary incentive of the Company's **____** As noted above, these are separate objectives where one element is based on financial performance (PSUs) and the other is based on tenure (RSUs). The Commission should not be confused by arguments made about the plan as a whole and should instead focus on the single RSU component of the plan, for which the Company is seeking recovery.

Q. Has the recovery of PSUs and RSUs been addressed in other jurisdictions?

A. Yes. I am most familiar with the regulatory treatment of Incentive Compensation at the Company's operating affiliate Ameren Illinois, regulated by the Illinois Commerce Commission ("ICC"). Similar to the Commission, the ICC has a long history of disallowing costs from the revenue requirement in rate cases for incentive compensation under certain circumstances. Specifically, the ICC ordered disallowances for incentive compensation costs like the Company's current PSUs that contain performance conditions tied to shareholder return or earnings per share.[3] The ICC, however, has allowed recovery of prudent and reasonable incentive compensation cost, including RSUs, as a part of the utility's total compensation cost, in utility rates.[4] Therefore, as noted above, RSUs are completely disconnected from any Ameren financial goals and the ICC allowed recovery of those costs.[5]

The Company and Ameren Illinois both utilize the same LTIP, including RSU compensation. Ameren Illinois has recovered its RSU costs in rates since its 2018 natural gas rate review and its 2019 electric formula rate review, shortly after RSUs were included in the LTIP. Clearly this outcome is due to the reasonableness of the incentive costs and the RSUs not being tied to a financial goal or financial metric, and the ICC's recognition that RSUs and PSUs are, in fact, different. In Ameren Illinois' most recent natural gas case,[6] the ICC recognized that:

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[3] *See,* ICC Docket No. 07-0507 (*"The Commission has consistently disallowed recovery of payouts that are tied to overall financial goals."*)
[4] *See, e.g.*, ICC Docket No. 15-0142, Order at 44 and ICC Docket No. 18-1775, Order at 82.
[5] *See,* ICC Docket Nos. 18-1775; 19-0436; 18-0463; and 20-0308.
[6] ICC Docket 20-0308.

> RSUs are stock units that vest over a defined period of time based solely on continued employment and are not subject to or based on financial metrics for the benefit of shareholders. The Commission holds that employee longevity provides a tangible benefit to ratepayers through reduced expenses and the creation of greater efficiencies in operations due to a more seasoned workforce.
>
> ICC Docket 20-0308, Order at 55-56 *citing* ICC Docket No. 18-1775, Order at 82.

Staff has not distinguished the RSUs from the PSUs in the long-term incentive plan. Staff disregards the fact that employee longevity provides a tangible benefit to customers through reduced expenses and the creation of greater efficiencies in operations due to a more seasoned workforce.

Q. Is there any element of Staff's position that would suggest it would recommend disallowance of RSU costs if those payments were made in cash rather than stock?

A. No. The Company would almost certainly be allowed to recover its RSU costs under an arrangement where it made those payments in cash rather than stock. It is unreasonable to believe that an experienced workforce does not add value to management and operational processes that benefit our customers, or that this benefit is somehow outweighed by the mere presence of stock in the plan. It is unreasonable to think that such an insignificant difference could result in the disallowance of more than $3 million of prudently incurred compensation costs.

Q. Why are the Company's RSU payments made in stock rather than cash?

A. Stock awards promote greater retention than cash awards, and retention is the purpose of the RSUs. In addition, as I mentioned previously, the Company regularly benchmarks its compensation arrangements against its peers. This is because we are competing against those peers to attract and retain our skilled employees. Differences from the benchmark (market data) could negatively impact our ability to hire or retain key employees and, as a result, undermine our attraction and retention strategy as well as lead to increased costs. Industry practice is to make such payments in stock, rather than in cash.

IV. EXCEPTIONAL PERFORMANCE BONUS

Q. Staff proposed a normalization of Exceptional Performance Bonus ("EPB") costs using a three-year average. Does the Company agree with this adjustment?

A. No. Staff does not provide any justification as to why normalization of the Company's EPB expense is appropriate. EPBs are a form of cash compensation for employees, similar to traditional payroll. Staff did not propose a normalization of payroll costs. Much like there is no logical justification for normalizing payroll, there is no logical rational for normalizing the Company's EPB expense, which is based on a percentage of annual payroll costs.

The EPB Budget is established annually based on a percentage of eligible employee base salaries. The EPB program allows leaders to reward employees when they provide outstanding results and/or do work that is above and beyond what is expected or required. Spot bonus programs, like the EPB program, are intended to be cost-effective programs that motivate employees, increase engagement, impact productivity, and provide retention for high performers, all of which benefit customers. Because the EPB budget is established annually based on base pay at the beginning of each year, normalizing the cost of a three-year period does not allow for appropriate recovery of the cost of this program.

V. SEVERANCE PAYMENTS

Q. Staff has proposed to disallow severance expenses. Does the Company agree with this adjustment?

A. No. Staff asserts that the Company will have cost savings by means of regulatory lag because the employees who are no longer employed are still included in current customer rates. It is not appropriate to apply ratemaking considerations to a single issue like severance. No savings exist after considering overall wages increased, as well as employment levels when compared to the Company's last rate review. Staff's recommendation of a wage rate increase in this case further demonstrates that on an overall basis net savings as compared to current rates do not exist.

Staff also asserts that severance payments are not a reoccurring cost; however, some level of ongoing severance costs is necessary and normal for the Company to incur in the normal course of business. As shown below, the Company has had direct severance costs or indirect severance cost from Ameren Services Company each of the last five years.

	2018	2019	2020	2021	2022
Ameren Services Company	$40,658	$496,900	$38,051	$59,578	$208,886
Ameren Missouri	$114,300	$159,500	$0	$170,600	$0

Additionally, severance is intended to be a safety net for employees who are displaced from their position due to a reduction in force, elimination of position, or change in strategic direction. This safety net encourages retention, which benefits customers as noted above with respect to other tenure-based programs.

If Staff's proposal is accepted, the allowed level of expense would fail to reflect a normal, ongoing level of severance expense and would thus understate the Company's revenue requirement.

Q. Does this conclude your rebuttal testimony?

A. Yes, it does.

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 Its Revenues for Electric Service.	)))	Case No. ER-2022-0337

AFFIDAVIT OF KELLY HASENFRATZ

STATE OF MISSOURI)
) ss
CITY OF ST. LOUIS)

Kelly Hasenfratz, being first duly sworn states:

My name is Kelly Hasenfratz, and on my oath declare that I am of sound mind and lawful age; that I have prepared the foregoing *Rebuttal Testimony*; and further, under the penalty of perjury, that the same is true and correct to the best of my knowledge and belief.

/s/ Kelly Hasenfratz
Kelly Hasenfratz

Sworn to me this 15th day of February, 2023.