

Exhibit No.:
Issues: Return on Equity and DSM
Witness: Billie S. LaConte
Sponsoring Party: Missouri Energy Group
Type of Exhibit: Surrebuttal Testimony
Case No.: ER-2011-0028
Date Testimony Prepared: April 15, 2011

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Union Electric Company d/b/a)
AmerenUE for Authority to File Tariffs Increasing) Case No. ER-2011-0028
Rates for Electric Service Provided to Customers)
In the Company's Missouri Service Area.)

SURREBUTTAL TESTIMONY

OF

BILLIE SUE LACONTE

ON BEHALF OF

MISSOURI ENERGY GROUP

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Union Electric Company d/b/a)
AmerenUE for Authority to File Tariffs Increasing) Case No. ER-2011-0028
Rates for Electric Service Provided to Customers)
In the Company's Missouri Service Area.)

Affidavit of Billie S. LaConte

STATE OF MISSOURI)
)
COUNTY OF ST. LOUIS)

Billie S. LaConte, being of lawful age and duly affirmed, states the following:

1. My name is Billie S. LaConte. I am a consultant in the field of public utility economics and regulation and a member of Drazen Consulting Group, Inc.
2. Attached hereto and made a part hereof for all purposes is my Surrebuttal Testimony consisting of Pages 1 through 9.
3. I have reviewed the attached Surrebuttal Testimony and hereby affirm that my testimony is true and correct to the best of my knowledge and belief.


Billie S. LaConte

Duly affirmed before me this 15th day of April, 2011.


Notary Public

My commission expires on August 7, 2013.



CAROL J. INSALACO
My Commission Expires
August 7, 2013
St. Louis County
Commission #08488213

Table of Contents

Return on Equity

Response to AMMO Witness Hevert Rebuttal Testimony	1
Response to MIEC Witness Gorman Rebuttal Testimony	5

Energy Efficiency

Response to AMMO Witness Davis Rebuttal Testimony.....	8
--	---

SURREBUTTAL TESTIMONY OF BILLIE SUE LACONTE

CASE NO. ER-2011-0028

1 Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

2 A Billie S. LaConte, 8000 Maryland Avenue, Suite 1210, St. Louis, Missouri.

3 Q ARE YOU THE SAME BILLIE SUE LACONTE THAT FILED DIRECT AND REBUTTAL
4 TESTIMONY IN THIS PROCEEDING?

5 A Yes, I am.

6 Q WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY IN THIS PROCEEDING?

7 A I shall address the rebuttal testimony filed by AMMO witness Mr. Robert Hevert, the
8 rebuttal testimony filed by MIEC witness Mr. Mike Gorman and the rebuttal testimony
9 filed by AMMO witness Mr. William Davis.

10 **RETURN ON EQUITY**

11 ***Response to AMMO Witness Hevert Rebuttal Testimony***

12 Q PLEASE DESCRIBE MR. HEVERT'S COMMENTS.

13 A Mr. Hevert disagrees with several aspects of my calculation of the appropriate RoE for
14 AMMO. They include:

- 15 • Assumed growth rates;
- 16 • Companies used to determine the RoE;

- 1 • Using a historical risk premium in my CAPM and risk premium analyses;
- 2 • Reliance on Value Line data;
- 3 • Calculation of dividend yields used in my DCF analyses; and
- 4 • My conclusions and characterization of the company's business risks.

5 **Q WHY DOES MR. HEVERT DISAGREE WITH YOUR GROWTH RATES?**

6 A Mr. Hevert does not disagree with the growth rates I used, but disagrees with my
7 application of those growth rates. Specifically, he does not agree that long-term growth
8 forecasts should be used in a single stage DCF analysis. My single stage DCF analyses
9 include several growth forecasts; I did not rely on one single-stage DCF analysis to
10 estimate AMMO's appropriate RoE. The growth forecasts I use represent analysts'
11 growth forecasts for each proxy company, an average of the analysts' growth forecasts
12 for all of the companies in the proxy group and a forecast long-term GDP growth rate.
13 The combination of these DCF analyses presents a fair estimation of the appropriate RoE
14 for AMMO.

15 **Q WHAT IS MR. HEVERT'S OBJECTION TO YOUR PROXY GROUP?**

16 A Mr. Hevert states that my selection did not consider certain financial and operational
17 parameters. However, he stated in his rebuttal that "while I do not necessarily agree
18 with all of Ms. LaConte's proxy companies, I *have included them in the Combined Proxy*
19 *Group*" (Rebuttal of Robert B. Hevert, Page 94, Lines 3-5, emphasis added).

1 Q WHAT IS MR. HEVERT'S OBJECTION TO YOUR CAPM, ECAPM AND RISK PREMIUM
2 METHODS?

3 A Mr. Hevert does not agree with the historical data I used for my CAPM, ECAPM and risk
4 premium methods as compared to the forecast data he used because he believes they
5 do not "properly reflect important market considerations." The historical data I used is
6 in addition to the forecast data used in my DCF analyses. Investors consider a number
7 of factors when estimating a company's expected return, including historical and
8 forecast data. This combination provides a reasonable estimation of AMMO's RoE.

9 Q PLEASE DISCUSS MR. HEVERT'S CRITICISM OF YOUR MULTI-STAGE ANALYSES AND
10 RELIANCE ON VALUE LINE DATA.

11 A Mr. Hevert's comments regarding my multi-stage DCF analyses state that the terminal
12 stage of my analyses represents 84.09% of the model's price estimate. The terminal
13 stage represents the long-term, therefore it is appropriate that it represents a large
14 portion of the model's price estimate. The analysts' growth forecasts that I used in the
15 multi-stage model represent the short- to near-term, or three to five years. Regarding
16 my use of Value Line data, Mr. Hevert objects because I only used Value Line data in my
17 multi-stage analyses, which he claims may lead to a potential bias. While it is true I
18 relied on Value Line data for my multi-stage analyses, the estimated RoE for AMMO is
19 based on a variety of methods using various analysts' forecasts and also historical data,
20 so there is no bias.

1 Q WHY DOES MR. HEVERT DISAGREE WITH THE DIVIDEND YIELDS USED IN YOUR
2 ANALYSES?

3 A Mr. Hevert disagrees with the method I used to calculate my dividend yields. He states
4 that my method does not recognize that dividend yields may change at any time during
5 the year, since dividends are paid quarterly. The dividend yield I used is based on an
6 average of actual dividend yields for 2010 and forecast dividend yields for 2011, which
7 does recognize any expected growth (or decrease) in the dividend yield. Although Mr.
8 Hevert disagrees with the method I used to calculate the dividend yield, he
9 acknowledges that “the average expected dividend yield...is not materially different
10 than the average expected dividend yield provided in (his testimony)” (Hevert Rebuttal,
11 Page 95, Lines 13-15).

12 Q SHOULD THE COMMISSION ADJUST AMMO’S ROE TO REFLECT THE HIGHER
13 REGULATORY RISK AND ITS RELIANCE ON COAL-FIRED GENERATION?

14 A No. The regulatory framework in Missouri has not changed since the previous rate case,
15 where no adjustment was made to recognize this risk. AMMO’s generation portfolio
16 has not significantly changed since the previous rate case. Again, no adjustment was
17 made to recognize this additional risk. Mr. Hevert is correct when he states that AMMO
18 is not seeking an environmental cost recovery mechanism in this case, only recovery of
19 its current environmental expenditures. The Company goes to great lengths to describe
20 expected environmental laws that may require billions of dollars of investment in the
21 next five years (Direct Testimony of Warner Baxter, Pages 5-6). While it is true, that

1 new environmental laws are expected, the Company had the option of applying for an
2 environmental cost recovery mechanism (ECRM), to alleviate some of the regulatory lag
3 associated with those investments. While my prior testimony stated that the Company
4 had asked for an ECRM in this case, upon further review I realized that the Company
5 opted not to ask for one in this rate case. Customers should not have to pay a higher
6 return on equity because the Company elected not to avail itself of this option.

7 **Q DO YOU AGREE WITH MR. HEVERT'S RECOMMENDED ROE?**

8 A No. His recommended RoE is too high. He has not changed his recommendation, even
9 though his revised multi-stage analyses result in a lower mid-point RoE (from 10.9% to
10 10.6%; Rebuttal Testimony of Robert B. Hevert, Page 8, Line 10, Table 2). Furthermore,
11 out of the four witnesses' recommendations, Mr. Hevert's recommended RoE is at least
12 120 basis points higher than the mid-point of the recommended range. Mr. Hevert is
13 the only witness that recommends a higher RoE for AMMO to account for the
14 Company's higher regulatory risk as compared to his proxy group and the Company's
15 reliance on coal-fired generation.

16 ***Response to MIEC Witness Gorman Rebuttal Testimony***

17 **Q WHAT IS MR. GORMAN'S ANALYSIS?**

18 A MIEC witness, Mr. Gorman, states that the long-term GDP growth factor I used in my
19 analysis is "calculated incorrectly and...it does not reflect the consensus economists' and
20 therefore investors' outlook for long-term GDP growth" (Rebuttal Testimony of Michael

1 Gorman, Page 26, Lines 22-23 and Page 27, Line 1). Mr. Gorman states that a more
2 realistic long-term GDP growth factor is one that is based on a consensus of economic
3 forecasts.

4 **Q DO YOU AGREE WITH MR. GORMAN?**

5 A No and yes. No, I do not agree that the long-term GDP growth factor I used is calculated
6 incorrectly, nor do I agree that it does not reflect investors' outlook for long-term GDP
7 growth. The long-term GDP growth factor I used is the same growth factor used by Mr.
8 Hevert. Although the long-term GDP growth factor I used is higher than the forecast,
9 that does not preclude it from reflecting investors' expectations. It is based on long-
10 term, historical data, which some investors may use to determine growth outlooks and,
11 subsequently, the expected return. I am not opposed to using a forecast long-term GDP
12 growth factor. I agree that some investors may use a forecast long-term growth rate
13 based on a consensus of economists, as Mr. Gorman points out.

14 **Q WHY DID YOU NOT INCLUDE AN ANALYSIS THAT EMPLOYS THE CONSENSUS FORECAST**
15 **OF LONG-TERM GDP GROWTH?**

16 A I used Mr. Hevert's growth forecast simply to provide a conservative estimate of
17 AMMO's RoE. My recommended range is 9.7-10.6%, which is based on several methods
18 that include forecast and historical data.

Table 1

Recommended Return on Equity

<u>Method</u>	<u>RoE</u>
DCF Method-Constant Growth (Analyst Growth)	10.5%
DCF Method-Constant Growth (GDP Growth)	10.6
DCF Method-Two-stage Growth (Analyst Growth)	10.1
DCF Method-Two-stage Growth (GDP Growth)	10.3*
Risk Premium Method with current rate	10.0
Risk Premium Method with forecast rate	9.7
CAPM	9.0
ECAPM	9.5%

*The estimated RoE in my direct testimony using this method was 10.4%. Due to a calculation error, I have revised my estimate to correct the error.

1 Substituting the forecast long-term GDP growth rate in my DCF calculations that use a
2 historical long-term GDP growth forecast does lower the estimated RoE. In my single-
3 stage DCF analysis, it lowers the estimated RoE from 10.6% to 9.8%. In my two-stage
4 DCF analysis, it lowers the estimated RoE from 10.3% to 9.5%. The overall effect is to
5 lower the high end of my recommended range from 10.6% to 10.5%.

6 **Q WHAT IS YOUR RECOMMENDATION TO THE COMMISSION REGARDING AMMO'S ROE?**

7 **A** As shown in the table above, my recommended RoE focuses on the DCF and risk
8 premium methods. Including the CAPM and ECAPM estimates would expand my
9 recommended range to 9.0% - 10.6%, with a mid-point of 9.8%. Traditionally, the
10 Commission has relied on DCF methods when authorizing a RoE. However, in the

1 Commission's Decision in Case No. ER-2010-0355, on April 12, 2011, the Commission
2 stated:

3 *The Commission may select its methodology in determining rates and*
4 *make pragmatic adjustments called for by particular circumstances. It*
5 *may employ a combination of methodologies and vary its approach from*
6 *case-to-case and from company-to-company. (File No. ER-2010-0355,*
7 *Report and Order, Page 123-124, Paragraph 38).*

8 The CAPM and ECAPM provide a reasonable estimate of AMMO's RoE, as well as to
9 check the reasonableness of the DCF and risk premium methods. As a check of
10 reasonableness, it is my opinion that an appropriate RoE for AMMO should be at the
11 lower end of my recommendation, that is, from 9.7% - 10.0%.

12 **ENERGY EFFICIENCY**

13 ***Response to AMMO Witness Davis Rebuttal Testimony***

14 **Q PLEASE DESCRIBE MR. DAVIS' PROPOSAL.**

15 **A** In his rebuttal testimony, Mr. Davis proposes to reduce residential sales by an additional
16 250,951 MWhs and reduce sales for SGS, LGS, SPS and LPS by an additional 227,678
17 MWhs (Rebuttal Testimony of William R. Davis, Page 13, Lines 15 and 17) to "reflect the
18 anticipated effects of its energy efficiency programs" (Davis Rebuttal, Page 13, Lines 13-
19 14). In addition, he proposes that "for classes with demand-related charges I propose
20 those demand units be reduced by the same percentage" (Davis Rebuttal, Page 6, Lines
21 21-23).

1 Q DO YOU HAVE ANY COMMENTS REGARDING MR. DAVIS' PROPOSAL?

2 A Yes. The adjustments to AMMO's billing units recommended by Mr. Davis should not be
3 allowed. The proposed adjustments include *forecast* effects of energy efficiency
4 programs that occur outside of the test year. The billing units that AMMO has used to
5 set rates in this case already include the effects of energy efficiency programs for the
6 test year. Mr. Davis recognizes this fact in his rebuttal testimony:

7 *This approach recognizes that the sales used to set rates do not reflect*
8 *anticipated savings from energy efficiency programs.* (Rebuttal
9 Testimony of William R. Davis, Page 6, Lines 9-10, emphasis added).

10 That is, the billing units used to set rates in this case have already been adjusted to
11 account for the effect of AMMO's energy efficiency programs.

12 Q WHAT IS YOUR RECOMMENDATION?

13 A The Company should not reduce its billing units any further. The test year includes the
14 effects of the energy efficiency program and AMMO should not be allowed to adjust its
15 billing units to reflect "anticipated effects of its energy efficiency programs", i.e., for
16 periods that fall outside of the test year.

17 Q DOES THIS CONCLUDE YOUR TESTIMONY?

18 A Yes.