Exhibit No.:	
Issue(s):	Capital Structure
Witness:	Darryl T. Sagel
Type of Exhibit:	Surrebuttal Testimony
Sponsoring Party:	Union Electric Company
File No.:	GR-2019-0077
Date Testimony Prepared:	July 10, 2019

MISSOURI PUBLIC SERVICE COMMISSION

FILE NO. GR-2019-0077

SURREBUTTAL TESTIMONY

OF

DARRYL T. SAGEL

ON

BEHALF OF

UNION ELECTRIC COMPANY

D/B/A AMEREN MISSOURI

St. Louis, Missouri
July, 2019

****<u>DENOTES CONFIDENTIAL INFORMATION</u>****

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SURREBUTTAL TESTIMONY

OF

DARRYL T. SAGEL

FILE NO. GR-2019-0077

Q. Please state your name and business address.

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

Q. Are you the same Darryl T. Sagel that filed rebuttal testimony in this proceeding?

A. Yes, I am.

I. PURPOSE OF TESTIMONY

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

A. My surrebuttal testimony in this proceeding responds to the rebuttal testimony of Jeffrey Smith, submitted on behalf of the Missouri Public Service Commission Staff ("Staff"), and the rebuttal testimony of Robert Schallenberg, submitted on behalf of the Office of Public Counsel ("OPC").

Q. Are you sponsoring any schedules in connection with your testimony?

A. Yes, I am sponsoring, and have attached to my surrebuttal testimony, the following schedule, which has been prepared under my direction:

- Schedule DTS-S1 – UBS Research: Regulatory Jurisdictional Rankings

II. RESPONSE TO STAFF WITNESS JEFFREY SMITH'S REBUTTAL TESTIMONY REGARDING RECOMMENDED ALLOWED CAPITAL STRUCTURE

Q. Mr. Smith suggests that the risk profiles of Ameren Missouri and Ameren Illinois are not substantively different to justify a higher equity ratio for Ameren Missouri, Smith Rebuttal, pg. 3. Do you agree?

A. No. As I discussed in my rebuttal testimony, the respective capital structures for Ameren Missouri and Ameren Illinois are managed independently, based on, among other factors, relative business risk. In the case of Ameren Illinois, maintenance of a lower common equity ratio relative to Ameren Missouri is currently reasonable based on Ameren Illinois' lower business risk profile.

Ameren Illinois solely operates lower-risk electric transmission and distribution businesses and natural gas delivery businesses while Ameren Missouri operates a vertically-integrated electric business and a modest natural gas delivery business. It is noteworthy that equity and debt investors in the public utilities sector and the rating agencies that rate public utility companies and their respective debt securities assign higher risk to the generation component of operations relative to electric transmission and distribution operations and gas delivery operations.

Furthermore, Ameren Missouri owns and operates a single-unit nuclear plant, the Callaway Nuclear Generating Station. While Ameren Missouri has successfully operated Callaway since 1984, such ownership is similarly perceived by investors and the rating agencies as adding incremental risk to Ameren Missouri relative to other utilities, such as Ameren Illinois, which own no nuclear generation.

Finally, Ameren Illinois' electric transmission and distribution businesses and natural gas delivery businesses operate under regulatory frameworks that are more business-friendly than Ameren Missouri. In the case of Ameren Illinois' electric transmission business, the regulatory framework includes an allowed return on equity ("ROE") of 10.82% (including a 50 basis point adder for participation in the Midcontinent Independent System Operator, Inc. regional transmission organization), forward-looking test years with annual reconciliation, and construction work in progress ("CWIP") in rate base. For Ameren Illinois' natural gas operations, the regulatory framework includes an allowed ROE of 9.87%, a forward test year approach, an infrastructure rider for qualifying capital investments made between rate cases, and revenue decoupling for residential and small non-residential customers. Ameren Illinois' electric distribution regulatory framework includes formula ratemaking, revenue decoupling and a constructive energy efficiency policy approach. In contrast, the Missouri ratemaking framework, while demonstrating improvement following the passage in 2018 of Senate Bill 564 and the related implementation of partial plant-in-service accounting, still utilizes a historic test year approach, exposing Ameren Missouri to regulatory lag, thereby resulting in a higher degree of regulatory risk.

Q. Are there independent sources that provide support for your statement that Ameren Illinois' business risk position is lower than Ameren Missouri's business risk position?

A. Yes. I would specifically point to recent commentary from the rating agencies that issue credit ratings and credit opinions on Ameren Missouri and Ameren Illinois. In addition, another independent agency, Regulatory Research Associates, Inc.

("RRA"), currently ranks Missouri's regulatory environment as worse than Illinois' regulatory environment.

Q. How do Ameren Missouri's credit ratings compare to Ameren Illinois' credit ratings?

A. Both Ameren Missouri and Ameren Illinois have issuer credit ratings from Standard and Poor's Ratings Services ("S&P") and Moody's Investor Services ("Moody's"). S&P, which generally utilizes a consolidated approach to rating Ameren Corporation (parent), Ameren Missouri, and Ameren Illinois, currently rates both Ameren Missouri and Ameren Illinois BBB+. In contrast, Moody's utilizes a "building block" rating approach to evaluate Ameren Corporation (parent), Ameren Missouri, and Ameren Illinois, and issuer ratings are developed individually for Ameren Missouri and Ameren Illinois. Based on this methodology, Ameren Missouri is currently rated one notch lower (Baa1) than Ameren Illinois (A3).

Q. Is there evidence that Moody's believes Ameren Missouri's generation position adds risk to its overall credit profile and contributes to its lower credit rating than Ameren Illinois?

A. Yes. As highlighted in its most recent credit opinion, dated March 29, 2019, Ameren Missouri's *Rating Methodology and Scorecard Factors* indicates a "Generation and Fuel Diversity" Score indicative of a Ba rating, lower than the Baa1 actual rating assigned to Ameren Missouri. This suggests that Ameren Missouri's generation mix on balance detracts from Ameren Missouri's rating. It is notable that Ameren Illinois' comparable "Generation and Fuel Diversity" Score is not applicable since Ameren Illinois owns no generation and therefore generation has no bearing on its A3 issuer rating. Furthermore, in the same Ameren Missouri report, Moody's states:

> **____**

Q. Is there evidence that Moody's views Ameren Missouri's regulatory environment as less supportive than Ameren Illinois' regulatory environment?

A. Yes. In its most recent March 29, 2019 credit opinion on Ameren Missouri, Moody's notes the following:

> **____

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Q. How does RRA rank the Missouri and Illinois regulatory environment?

A. RRA operates as an independent research organization that provides research and consultation services to investment, corporate, and regulatory communities regarding public utility regulation and critical regulatory issues and actions in the electric and gas utility sectors.

As part of its research, RRA ranks each state regulatory jurisdiction based on a nine-point scale. RRA maintains three principal rating categories for regulatory climates: Above Average, Average, and Below Average. Within the principal rating categories, the numbers 1, 2, and 3 indicate relative position, with the designation 1 indicating a stronger rating, 2 indicating a mid-range rating, and 3 a weaker rating. Within this framework, "Above Average / 1" is the best possible ranking, while "Below Average / 3" is the worst possible ranking. The evaluations are assigned from an investor perspective and indicate the relative regulatory risk associated with the ownership of securities issued by the jurisdiction's utilities. The evaluation reflects RRA's assessment of the probable level and quality of the earnings to be realized by the state's utilities as a result of regulatory, legislative, and court actions.

Currently, RRA ranks Missouri "Average / 3," which is lower than Illinois' comparable rating of "Average / 2." RRA specifically states that "Missouri regulation is somewhat more restrictive than average from an investor perspective", while "Illinois regulation is relatively balanced from an investor perspective." I would also note that RRA changed its ranking of Missouri in June 2019 from "Below Average / 1", primarily as a result of the passage of Senate Bill 564.

Q. Mr. Smith suggests that a more reasonable allowed capital structure for Ameren Missouri would be similar to Ameren Illinois, which caps the common equity ratio at 50%. Do you agree?

A. No. Based on the differences in risk profile between Ameren Missouri and Ameren Illinois I described above, I believe it is more reasonable for Ameren Missouri to maintain a higher common equity ratio than Ameren Illinois.

In addition, and as highlighted in my rebuttal testimony, Mr. Smith's approach would set rates based not on what the Missouri Public Service Commission (the "Commission") has determined to be the discrete financing needs and requirements of Ameren Missouri, but based on what utilities and/or their regulators in other jurisdictions have decided should be done to meet the financial requirements of their distinct operations. This approach disregards protection or insulation of Ameren Missouri from the activities of its affiliates, and is inconsistent with the Commission's obligation to make decisions for Missouri utilities, rather than delegating the task out to other regulators.

I would also further reference my rebuttal testimony which refutes Mr. Smith's notion that Illinois legislation caps Ameren Illinois' equity ratio at 50%. Rather, the Future Energy Jobs Act, Illinois legislation that become effective June 1, 2017, established that an equity ratio up to and including 50% will be deemed reasonable. However, the legislation does not preclude Ameren Illinois from filing for a capital structure that uses an equity ratio greater than 50% if Ameren Illinois were able to justify such a capital structure (i.e., if its risk profile increased).

Q. Mr. Smith intimates – Smith Rebuttal, Pg. 2 - that as a result of the passage of Senate Bill 564 ("SB 564"), equity investors are placing a premium on Ameren's stock due to lower business risk at Ameren Missouri. How do you respond?

A. While I agree that the passage of SB 564 and the related implementation of partial plant-in-service accounting has reduced Ameren Missouri business risk relative to the framework in place prior to the legislation, I do not believe that such passage is solely responsible for Ameren trading at a premium.

Mr. Smith does not identify which metric he is relying upon to support his assertion that investors are placing a premium on Ameren's stock due to lower business risk at Ameren Missouri, nor does he indicate the comparison set. He only references unnamed research analyst reports to support his case.

Ameren does track its stock price performance over time relative to identified corporate peers and the PHLX Utility Sector Index (the "UTY"). In addition, we track Ameren's forward price-to-earnings ("P/E") multiple relative to peers and the UTY over time given that we believe that public utility sector equity investors rely predominantly on this metric to inform their investment decisions. Currently, Ameren's stock does trade at a next-12-month ("NTM") P/E multiple premium to the average of identified peer regulated companies, as well as the UTY. However, notably, Ameren's stock also happened to trade at a NTM P/E multiple premium to these two comparable sets in the months prior to passage of SB 564. Therefore, it is not reasonable to suggest that investors are placing a premium on Ameren's stock due specifically to legislative changes in Missouri and their impact on business risk. Ameren's stock has indeed performed well in the lead-up to, and following passage of, SB 564, though I would attribute that performance more to investors eliminating the historic discount ascribed to Missouri jurisdictional activities as a result of the enhanced growth opportunity created following the passage of SB 564 rather than such investors assigning a premium to the inherent business risks of the jurisdiction. Currently, I believe that Ameren's NTM P/E multiple premium is still due predominantly to its activities in Illinois and Federal Energy Regulatory Commission-regulated transmission.

It is noteworthy that equity analysts that publish research on Ameren's stock also tend to focus on Ameren's P/E multiple relative to their identified peer sets. Based on equity research that I reviewed recently, many analysts, in establishing their price targets, do suggest that Ameren's stock warrants a P/E multiple premium, though they attribute such a suggested premium to Ameren's higher-than average earnings-per-share ("EPS") growth rate within generally constructive jurisdictions. However, only a couple of analysts specifically cite Ameren Missouri as distinctly warranting a premium, and that premium is justified based on investment and growth prospects in the state, rather than its fundamental business risk position. For instance, I would highlight recent research from UBS included as Schedule DTS-S1, which advises that Missouri is a Tier 3 regulatory jurisdiction (out of five tiers, with Tier 1 the best and Tier 5 the worst) as compared to the Federal Energy Regulatory Commission, which is a Tier 1 jurisdiction and Illinois, which is a Tier 2 jurisdiction. Such rankings, similar to aforementioned state regulatory rankings from RRA, suggest that Missouri is not, in fact, a premium jurisdiction from an investment standpoint as Mr. Smith proposes.

Q. Mr. Smith reiterates assertions from his testimony in the Staff Cost of Service Report submitted in this proceeding that Ameren Missouri's capital structure is not appropriate for ratemaking purposes due to Ameren's increased holding company leverage, and that rates should instead be based on a recommended 50% cap on Ameren Missouri's common equity ratio. Do you agree?

A. I strongly disagree with Mr. Smith's position and believe that my rebuttal testimony in this proceeding, and supported by Ms. Weber's direct testimony in this proceeding, still adequately reflects my position that Ameren Missouri's actual capital structure is appropriate and reasonable for purposes of setting rates in this proceeding. As listed in the Table 1 below, at the true-up date of May 31, 2019, Ameren Missouri's actual capital structure was 46.941% long-term debt, 1.014% preferred stock, and 52.045% common equity.

Table 1

($ in millions)

As of May 31, 2019

	Amount	Percent of Total
Long-Term Debt	$3,790	46.941%
Short-Term Debt	$0	0.000%
Preferred Stock	$82	1.014%
Common Equity	$4,202	52.045%
	$8,073	**100.000%**

III. RESPONSE TO OPC WITNESS ROBERT SCHALLENBERG REBUTTAL TESTIMONY REGARDING AFFILIATE TRANSACTIONS

Q. To what portion of Mr. Schallenberg's rebuttal testimony do you intend to respond?

A. My testimony relates to Mr. Schallenberg's recommendation that Ameren Missouri should not be allocated costs related to Ameren Corporation (parent) Board of Directors and shareholder services activities. My colleague, Laura Moore, is responding to other issues raised by Mr. Schallenberg in his rebuttal testimony related to affiliate transactions.

Q. Are Ameren (parent) Board of Director costs and investor services costs appropriately charged to Ameren Missouri?

A. Yes they are. Mr. Schallenberg provides no credible basis in his testimony to support exclusion of these expenses from Ameren Missouri's cost of service other than stating that the holding company entirely owns Ameren Missouri (i.e., Ameren Missouri has no independent shareholders) and that Ameren Missouri has no independent Board of Directors.

Currently, Board of Director expenses are allocated across each of Ameren's subsidiaries using the general allocator. This is an entirely appropriate allocation method because the Board of Directors exists to serve all of the Ameren business units, not just the holding company. Shareholder listing requirements for any public company necessitate certain governance procedures be undertaken, including the formation of a Board of Directors with a quorum of independent directors. Board of Director expenses are normal and customary costs of service, and absent the holding company structure (e.g., if Ameren Missouri were a stand-alone public company), there would be a Board of Directors, and associated costs, for Ameren Missouri. The Board of Directors provide oversight and guidance across many important aspects of Ameren Missouri's business, including monitoring and assessing its operational and financial performance, supporting budget analysis, and evaluating long-term capital planning. Given the importance of Ameren's Board of Directors to the successful operations of Ameren Missouri, there is no reasonable basis for the exclusion of such costs from Ameren Missouri's revenue requirement.

Similarly, as a publicly-traded company, Ameren relies upon its shareholders to support ongoing funding of its equity requirements. While Ameren has not been a frequent issuer of equity securities in recent years, having access to equity capital at all times to support subsidiary funding needs, including Ameren Missouri's, is a critical element to maintaining financial strength and solid credit ratings. Since Ameren (parent) owns 100% of the stock of Ameren Missouri, and because Ameren, as a policy, does not fund equity capital into Ameren Missouri with short-term or long-term debt, Ameren Missouri has no ability to raise equity capital on its own and therefore must depend upon Ameren (parent) to provide access to requisite equity capital. Shareholder services expenses are normal and customary costs of service for any publicly-traded company, and absent the holding company structure (e.g., if Ameren Missouri were a stand-alone public company), there would be shareholder service requirements, and associated costs, for Ameren Missouri. Given the importance of Ameren's shareholder services to Ameren Missouri's financial position, there is no reasonable basis for the exclusion of such costs from Ameren Missouri's revenue requirement.

IV. RESPONSE TO OPC WITNESS ROBERT SCHALLENBERG REBUTTAL TESTIMONY REGARDING CAPITAL STRUCTURE

Q. Mr. Schallenberg raises two issues regarding Ameren Missouri's proposed capital structure. His first issue mentions the discrepancy between the amount of long-term debt as of June 30, 2018 identified in Ameren Missouri witness Brenda Weber's testimony versus the amount of long-term debt as of that same date recorded in Ameren Missouri's second quarter 10-Q filing with the Securities and Exchange Commission ("SEC"). Can you explain what causes the difference between the two amounts?

A. The long-term debt referenced in Ms. Weber's direct testimony is based upon the methodology historically used and affirmed by the Commission to calculate Ameren Missouri's regulatory capital structure. Specifically, Ms. Weber's calculation applies various adjustments to the SEC-reported long-term debt balance, including eliminating amounts outstanding under Ameren Missouri's capital lease obligations (Audrain and Peno Creek Chapter 100 Tax Arrangements) and losses incurred associated with reacquired debt. Table 2 below provides a reconciliation of the balance of long-term debt shown in the SEC Form 10-Q filing with the regulatory balance of long-term debt identified in Ms. Weber's testimony.

Table 2

($ in millions)

As of June 30, 2018		
		Balance
SEC Form 10-Q Balances:		
Current maturities of long-term debt	$	534
Long-term debt, net		3,668
Total long-term debt	$	4,202
Regulatory adjustments:		
Capital leases	$	(276)
Loss on reacquired debt		(60)
Regulatory total long-term debt (per Ms. Weber's direct testimony)	$	3,867

Q. Mr. Schallenberg's second issue relates to a question whether Ameren Missouri's equity balance reflects an element of Ameren (parent) debt funding. How do you respond?

A. As I indicated in my rebuttal testimony in this proceeding, Ameren does not, as a policy, infuse common equity into Ameren Missouri with proceeds from long-term or short-term debt issuances. Rather, Ameren common equity infusions have been specifically funded by Ameren common equity issuances to third-party investors. The most recent infusion of common equity into Ameren Missouri by Ameren, in September 2009 in the amount of $436 million, was sourced directly from an external Ameren common stock offering in September 2009. The only other cash transfers from Ameren to Ameren Missouri since that September 2009 infusion have been modest non-discretionary tax-related contributions. These contributions are a function of a consolidating tax-allocation agreement among Ameren (parent) and its subsidiaries, including Ameren Missouri, and the contributions are typically promptly returned by Ameren Missouri to Ameren (parent) through subsequent dividend distributions, such that there is no net impact on Ameren Missouri's equity balance.

Q. Mr. Schallenberg notes that in recent SEC filings (10-K and 10-Q), the combined equity balances of Ameren Missouri and Ameren Illinois exceed Ameren (parent) equity balances, while Ameren's consolidated debt exceed the combined debt balances of Ameren Missouri and Ameren Illinois. Can you explain these differences?

A. Since year-end 2017, based on financials contained in quarterly and annual SEC filings, the combined equity balances of Ameren Missouri and Ameren Illinois have exceeded Ameren (parent) equity balances. This was not the case in SEC filings prior to the 2017 10-K. There are three key factors that have disproportionately impacted Ameren's (parent) equity ratio relative to the equity ratios of its regulated subsidiaries over the past several years.

First, Ameren (parent) took significant non-cash charges related to the revaluation of deferred taxes resulting from a December 2017 change in federal law that decreased the federal corporate income tax rate (the benefit of which was proportionately passed through to Ameren Missouri and Ameren Illinois customers). These charges totaled $154 million in 2017 and an additional $13 million in 2018, with a disproportionate amount of the charges impacting Ameren's (parent) retained earnings as opposed to Ameren Missouri's and Ameren Illinois' retained earnings.

Second, Ameren Illinois' equity capital position has been recently supported by capital contributions from Ameren (parent) funded with short-term and long-term Ameren (parent) debt.

And, third, Ameren (parent) has declared and paid dividends to its common shareholders over the past several years at levels that are well in excess of the combined dividend distributions received from Ameren Missouri and Ameren Illinois. This is a function of these two subsidiaries reinvesting significant operating cash flow and retained earnings into their long-term regulated assets.

The result of these three primary factors, as shown in Table 3 below, has been a greater pace of increase in the equity balances of Ameren Missouri and Ameren Illinois relative to Ameren (parent).

Table 3

($ in millions)

	As of December 31,			% Change
	2016	**2017**	**2018**	**2016-2018**
SEC Form 10-K Balances:				
Ameren (parent) Common Equity	$ 7,103	$ 7,184	$ 7,631	7.4%
Ameren Missouri / Ameren Illinois Common Equity	6,982	7,249	7,861	12.6%
Difference	*$ 121*	*$ (65)*	*$ (230)*	

Mr. Schallenberg is also correct that Ameren's consolidated long-term debt balance exceeds the combined long-term debt balances of Ameren Missouri and Ameren Illinois. I would note that, in addition to comprising Ameren Missouri's and Ameren Illinois' long-term debt balance, the Ameren consolidated long-term debt balance includes $700 million of Ameren holding company long-term debt, which has been used to refinance $425 million of holding company debt that historically supported Ameren Energy Resources Company activities prior to its divestiture in 2013, and to support financing of Ameren Illinois and Ameren Transmission Company of Illinois ("ATXI") capital investment activities. As indicated previously, none of this holding company debt has been used for capital contributions to Ameren Missouri. Furthermore, Ameren's consolidated long-term debt balance includes $450 million of ATXI senior notes that have directly supported ATXI's electric transmission development program.

Q. Does this conclude your surrebuttal 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 Increase Its	)	File No. GR-2019-0077
Revenues for Natural Gas Service.	)	

AFFIDAVIT OF DARRYL T. SAGEL

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

Darryl T. Sagel, being first duly sworn on his oath, states:

1. My name is Darryl T. Sagel. I work in the City of St. Louis, Missouri, and I am employed by Union Electric Company d/b/a Ameren Missouri as Vice President and Treasurer.

2. Attached hereto and made a part hereof for all purposes is my Surrebuttal Testimony on behalf of Union Electric Company d/b/a Ameren Missouri consisting of 17 pages and Schedule(s) DTS-S1, all of which have been prepared in written form for introduction into evidence in the above-referenced docket.

3. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded are true and correct.

Darryl T Sagel
Darryl T. Sagel

Subscribed and sworn to before me this 9th day of July, 2019.

Geri A. Best
Notary Public

My commission expires:

GERI A. BEST
Notary Public - Notary Seal
State of Missouri
Commissioned for St. Louis County
My Commission Expires: February 15, 2022
Commission Number: 14839811

Regulatory Jurisdictional Rankings – Location Matters

Our current rankings are below, including Canadian provinces that regulate the subsidiaries of publicly traded utilities.

TIER 1	TIER 2	TIER 3	TIER 4	TIER 5
Potential		Nova Scotia		
		Kentucky		
FERC		North Dakota		
		South Carolina		
		Washington		
		Missouri		
		Oregon		
		Pennsylvania		
		Massachusetts		
		Delaware		
		Minnesota		
	Illinois	New Jersey	Mississippi	
	Arkansas	Wyoming	Kansas	
Florida	British Columbia	Rhode Island	New Hampshire	Nevada
Georgia	Indiana	Tennessee	Oklahoma	Ontario
Michigan	Ohio	Alberta	Alaska	New Mexico
Wisconsin	Virginia	Newfoundland & Labrador	Arizona	New York
Alabama	Louisiana	Prince Edward Island	South Dakota	Montana
Colorado	Idaho	West Virginia	California	District of Columbia
North Carolina	Texas	Connecticut	Hawaii	Maine
Utah	Iowa	Nebraska	Maryland	Vermont

Legend: Ameren | Moving Up | Moving Down

UBS

Source: Canadian Provincial Regulatory Websites, S&P Global Market Intelligence, FactSet, JD Power, UBS estimates