Exhibit No:	**___**
Issue:	**Capital Structure and Rate of Return (ROR)**
Witness:	**Adam Woodard**
Type of Exhibit:	**True-Up Rebuttal**
Sponsoring Party:	**Spire Missouri Inc.**
Case No.:	**GR-2021-0108**
Date Testimony Prepared:	**August 16, 2021**

SPIRE MISSOURI INC.

CASE NO. GR-2021-0108

TRUE-UP REBUTTAL TESTIMONY

OF

ADAM WOODARD

AUGUST 16, 2021

** Denotes Confidential Information **

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TRUE-UP REBUTTAL TESTIMONY OF ADAM WOODARD

I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Adam Woodard and my business address is 700 Market, St. Louis, MO 63101.

Q. ARE YOU THE SAME ADAM WOODARD WHO FILED REBUTTAL, SURREBUTTAL AND TRUE-UP DIRECT TESTIMONY IN THIS CASE?

A. Yes.

II. PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my testimony is to respond to the recommendations regarding capital structure and return on equity ("ROE") made by the Office of the Public Counsel ("OPC") witness Dave Murray in his True-Up Direct Testimony.

III. CAPITAL STRUCTURE

Q. DOES OPC'S WITNESS DAVID MURRAY PROVIDE AN UPDATED ANALYSIS OF THE COST OF ALL CAPITAL COMPONENTS IN HIS TRUE-UP DIRECT TESTIMONY?

A. No. Mr. Murray states that he analyzed changes to the capital structures of Spire Inc. and Spire Missouri including the cost of capital related to all capital components <u>except</u> common equity.[1] This is a significant omission on the part of the OPC. Indeed, Mr. Murray's ROE recommendation is based in part on information that extends back well before the inception of this current proceeding. He repeatedly cites the last Empire rate

[1] Murray True-Up Direct, p.1, line 12

case proceeding as the basis for his current recommendation. Mr. Murray's direct testimony in the last Empire proceeding was filed on January 15, 2020 based on market conditions in 2019.

Specifically, I disagree with the OPC's recommended capital structure of 48.00% long-term debt, 7.00% short-term debt and 45.00% equity which is based on a misleading interpretation of rating agency methodology; instead, I recommend that the Commission order a capital structure of 45.72% debt and 54.28% equity which is more appropriate for the Company as a stand-alone utility. This recommendation is also in line with past Commission practice as highlighted by the principles cited by the Commission in Spire's last rate proceeding, the Staff's recommendation in this case and my previously filed Rebuttal and Surrebuttal Testimony. Secondly, the Company maintains its position that a 9.95% ROE is more appropriate as reflected in the Direct, Rebuttal, and Surrebuttal Testimony of Company witness Dylan D'Ascendis.

Q. MR. MURRAY STATES THAT SPIRE MISSOURI UPDATED ITS CAPITAL STRUCTURE TO TARGET A CAPITAL STRUCTURE CONSISTENT WITH THAT WHICH THE COMMISSION AUTHORIZED IN CASES NOS. GR-2017-0215 AND GR-2017-0216. (MURRAY TRUE-UP DIRECT, PG 1.) IS THIS TRUE?

A. Yes. More precisely Spire Missouri updated its capital structure *in accordance* with the Commission's report and order in the last Spire rate proceeding. Mr. Murray disagrees with past Commission's decisions and offered relatively weak arguments challenging some of the finding of facts in the last report and order in prior testimony[2]. However,

[2] Murray Rebuttal pages 4-7. See also Woodard Rebuttal Testimony, pgs. 6-7; Woodard Surrebuttal Testimony pgs. 10-13.

Mr. Murray uses these same points in his testimony in the Empire electric rate proceeding to distinguish Empire from Spire Missouri[3].

Spire Missouri recommends the recognition of its actual capital structure based on all of the relevant finding of facts ("FOF") and conclusions of law provided to it by the Commission in its last report and order, as these facts remain true for Spire Missouri today[4]:

- Spire Inc. continues to hold public utilities which are regulated in other states (FOF #4)
- The recommendation is the actual capital structure on the true-up date (FOF#6)
- Spire Missouri continues to have an independently determined capital structure: Spire Missouri does not guaranty the obligations of the parent or any other affiliate and the Commission continues to approve any long-term debt issuance[5] (FOF#7)
- Spire Missouri's stand-alone capital structure continues to support its own bond rating (FOF#8)
- Spire Missouri's capital structure ratios are consistent with the capital structure in its last rate case (FOF#9)

[3] ER-2019-0374, Murray Surrebuttal Testimony, pgs. 17-19.

[4] GR-2017-0215 / GR-2017-0216, Amended Report and Order, pages 35-44.

[5] It should be noted that the OPC advocated *limiting* Spire Missouri's long-term debt authorization request in the last debt authorization process (which such limitation was ultimately accepted by the Commission) while they are advocating *expanding* Spire Missouri's long-term debt in the current proceeding.

- Spire Missouri's capital structure ratios as of the true-up date continue to be based upon the actual capital structure that finances the assets and operations of the public utility for which the Commission is setting rates (FOF#10)
- Spire Inc.'s capital structure continues to fund capital that has not been directly used to fund investments at Spire Missouri: it includes the common equity of other public utilities and unregulated operations (FOF#11)
- The recommended equity ratio is in the range of the five-year average common equity ratios of the proxy natural gas companies (FOF#25)
- The Commission specifically rejects a goodwill balance adjustment and states that the goodwill balance has been removed from rate base (Conclusions of Law)

Spire Missouri continues to manage its capital structure in accordance with the principles outlined by the Commission in its last rate proceeding while also supporting the best interests of the ratepayers. One example of the capital structure providing this support occurred during the true-up period. Winter Storm Uri and the resulting surge in natural gas pricing created significant operational and financial impacts on gas utilities throughout the region. Several utilities were downgraded by the rating agencies. Spire Missouri's rating was not downgraded. The flexibility provided by its capital structure assisted Spire Missouri in weathering the financial impacts of Winter Storm Uri.

Q. DID OPC'S ERRATA SHEET FILED ON JULY 28, 2021 EXPLAIN THE BASIS FOR THE CORRECTIONS THAT WERE MADE?

A. No. The errata sheet was filed without explanation.

Q. MR. MURRAY STATES THAT <u>SPIRE INC.</u> ISSUED AN ADDITIONAL $250 MILLION OF SHORT-TERM DEBT TO FINANCE HIGHER GAS COSTS RELATED TO WINTER STORM URI DURING THE TRUE-UP PERIOD. (MURRAY TRUE-UP DIRECT, PG 2. *Emphasis added.*) IS THIS ACCURATE?

A. No. <u>Spire Missouri</u> entered into a $250 million 364-day term loan to partially finance higher gas costs resulting from Winter Storm Uri. Also, <u>Spire Missouri</u> issued $305 million of 30-year first mortgage bonds during the true-up period. Spire Missouri's capital structure is part of the consolidated capital structure of Spire Inc.

Q. ARE THE EQUITY UNITS ISSUED BY SPIRE INC. RECOGNIZED AS A SPECIFIC COMPONENT OF ITS CAPITAL STRUCTURE?

A. No. The equity units are properly included in long-term debt under generally accepted accounting principles ("GAAP"). As stated in previous testimony[6] the cost of the equity units, specifically the debt host, is contained within Spire Inc.'s cost of long-term debt.

Q. ARE THE RATIOS INCLUDED IN SCHEDULE DM-TD-2 HC CORRECT?

A. No. ** [redacted] ** The schedule offered by Mr. Murray only

[6] Woodard Surrebuttal, page 15, line 2.

serves to confuse and is contrary to how this data should be treated under GAAP and was addressed by the Commission in Spire's last report and order[7].

Q. MR. MURRAY STATES THAT SPIRE INC.'S SHORT-TERM DEBT RATIO AS OF MAY 31, 2021 is ** [redacted] **. (MURRAY TRUE-UP DIRECT, PG 3.) IS THAT TRUE?

A. Yes, assuming current maturities of long-term debt are counted as long-term debt. Spire Inc.'s short-term debt as of May 31, 2021 is ** [redacted] ** which accounts for ** [redacted] ** of the total short- and long-term capitalization. It is also true that Spire Missouri's short-term debt as of May 31, 2021 is ** [redacted] ** which accounts for ** [redacted] ** of its short- and long-term capital structure and ** [redacted] ** of Spire Inc.'s capital structure. All of Spire Inc.'s consolidated short-term debt is attributable to Spire Missouri. Much of this short-term debt is attributable to deferred gas costs resulting from Winter Storm Uri. Spire Missouri has addressed the status of these balances with Staff and OPC and would like to refinance these into long-term debt immediately once an agreement on recovery has been reached.

Q. IS THE COMMISSION'S CUSTOMARY "POINT IN TIME" ANALYSIS A MANIPULATION OF SPIRE MISSOURI'S SHORT-TERM DEBT BALANCES FOR PURPOSES OF THE TRUE-UP PERIOD (MURRAY TRUE-UP DIRECT, PG. 7.)?

A. No. Mr. Murray is implying that Spire Missouri's approach is wrong by simply following historical Commission practice of using the 'point in time' analysis. The three-year average approach was rejected by the Commission in the Company's last rate case

[7] GR-2017-0215/GR-2017-0216 Amended Report and Order.

as noted in the Commission's report and order when referencing the balance of short-term assets relative to short-term debt:

> "Mr. Murray's proposal to add short-term debt to the capital structure ignores this fact by using a three-year average rather than the customary 'point in time' analysis of short-term debt"[8].

Spire Missouri has followed the Commission's "point in time" analysis as outlined in the report and order in its last rate proceeding, in this current proceeding, and would ask that this method be supported by the Commission on a consistent and prospective basis. The "point in time" analysis recognizes the dynamic that some short-term assets are transitory (like deferred gas costs) and are never intended to be capitalized while other short-term assets (like CWIP) will be capitalized at some point in the future but often not immediately placed into rate base. Mr. Murray's recommendation of a three-year average approach would essentially create a retroactive application of the treatment of the Company's short-term debt that is inconsistent with what the Commission has previously ordered. The consequences of his recommendation would result in penalizing the Company for managing its short-term debt based on the Commission's guidance in the Company's last rate case. If the Commission is reconsidering its customary analysis of short-term debt, Spire Missouri would request to be informed *before* entering a new rate cycle so it can manage it short-term assets and liabilities accordingly.

[8] GR-2017-0215 / GR-2017-0216, Amended Report and Order page 45 (also referenced on page 42).

Q. DOES SPIRE INC.'S CAPITAL STRUCTURE INCLUDE HYBRID SECURITIES THAT ARE ALLOCATED TO DEBT AND EQUITY BY THE RATING AGENCIES?

A. This question as posed in Mr. Murray's True-Up Testimony is not accurate[9]. Mr. Murray only cites the portions of the methodology that is supportive of his position and fails to address the rest of the rating agency reconciliation. Both Moody's and Standard & Poor's *reconcile* a rated company's entire financial statements according to their published methodology[10]. These reconciliations include recasting components of the balance sheet but also include significant adjustments to the income statement and cash flow statement. This has been a longstanding practice of the rating agencies and their oft cited metrics are derived from these reconciliations to a company's financial statements. Moody's and Standard & Poor's make significant reconciliations to the financial statements of both Spire Inc. and Spire Missouri in rating each of them individually. This requires a considerable amount of engagement by Spire Inc. and Spire Missouri as there is not consistent agreement between the rating agencies and the companies on how various reconciliations are to be applied. This information has been provided to the OPC through data requests in this proceeding and pursuant to the Company's last debt authorization order. Mr. Murray conveniently cites the part of these reconciliations that suits his purposes but ignores the rest. This is misleading. One notable example of this is the fact

[9] Murray True-Up Testimony, page 4, lines 5-6.

[10] Moody's, Financial Statement Adjustments in the Analysis of Non-Financial Corporations, August 9, 2018; Moody's, Hybrid Equity Credit, April 10, 2018; Standard & Poor's, Corporate Methodology: Ratios and Adjustments, April 1, 2019; Standard & Poor's, Hybrid Capital Handbook, September 15, 2008; Standard & Poor's, Hybrid Capital: Methodology and Assumptions, July 1, 2019.

that both rating agencies impute additional long-term debt to the extent that the pension is less than 100% funded. Spire Missouri's pension is not 100% funded and the OPC did not support Spire's filing position to fully fund it. Rating agency methodology imputes additional long-term debt given these circumstances, but this "debt" is not cited by Mr. Murray in his testimony.

It should be made abundantly clear that these rating agency reconciliations do NOT purport to be GAAP and the agencies themselves would reject any suggestion otherwise. Spire Missouri does not endorse Mr. Murray's misinformed attempt to alter its capital structure based upon selective treatment of rating agency methodology. Spire takes rating agency concerns into account when making corporate finance decisions but is certainly not governed by their methodology and metrics as Mr. Murray suggests.

IV. RATE OF RETURN

Q. MR. MURRAY RECOMMENDS THE COMMISSION REJECT THE COMPANY'S INCLUSION OF COMMON EQUITY FLOTATION COSTS CLAIMING RECOVERY OF FLOTATION COSTS ARE PROHIBITED AS PART OF THE REPORT AND ORDER RELATING TO THE COMPANY'S ACQUISITION OF MGE. (MURRAY TRUE-UP DIRECT, PGS. 4-5). HAS THE COMMISSION CONSIDERED FLOTATION COSTS IN THE PAST WHEN AUTHORIZING A RETURN ON EQUITY AND SHOULD IT CONSIDER THEM IN THIS PROCEEDING?

A. Yes. The Commission adjusted for flotation costs in Spire's last rate proceeding[11] which is difficult for Mr. Murray to reconcile in his statement accusing Spire Missouri of

[11] GR-2017-0215 / GR-2017-0216, page 31.

violating the Commission's Order. Once again, Mr. Murray is misconstruing the facts, and I disagree with the assertion that Spire Missouri is prohibited from including flotation costs based on the Report in Order in Case No. GM-2013-0254.

Mr. D'Ascendis provides an excellent explanation in his Direct Testimony of flotation costs and why they should be recovered through a rate of return adjustment[12]. These costs are real and are not accounted for in any of the models offered by Mr. Murray or Dr. Won or Mr. D'Ascendis. The costs for the issuance of permanent capital are charged to capital accounts and are not expensed on a utility's income statement. Recovery of capital investment is related to the expected useful life of such investment and equity is perpetual capital (as is assumed in discounted cash flow models). Historical flotation costs are a permanent loss of investment to a utility and should be accounted for when setting an authorized return on equity regardless of when such equity has been placed with investors. The great majority of a utility's flotation costs are incurred prior to a given test year but remains part of the cost structure during the test year and into the future. Mr. Murray would have the Commission believe that Spire Missouri's equity is not perpetual and issued without cost. This is simply not the case.

Q. IS SPIRE MISSOURI'S RECOMMENDATION OF A FLOTATION COST ADJUSTMENT TO ITS ALLOWED RETURN ON EQUITY AN ENDORSEMENT OF APPLYING SPIRE INC.'S CONSOLIDATED CAPITAL STRUCTURE AND CAPITAL COSTS TO SPIRE MISSOURI?

A. No. Mr. Murray argues that the Company's testimony recognizes Spire Inc.'s security issuances are not distinguishable for purposes of capitalizing Spire Missouri. Spire Inc.

[12] D'Ascendis Direct Testimony; Pages 45-48.

has not requested recovery of the cost of any debt outside Spire Missouri. However, Spire Missouri's debt is a component of the consolidated debt structure of Spire Inc. It would be awkward to ask the Commission for recovery of the cost of debt for Spire Alabama. This is certainly a distinguishing factor. Spire Missouri does not issue its own equity to third-party investors and has not received equity from Spire Inc. for a number of years. However, equity is perpetual capital which makes the recovery of related flotation costs distinguishable from when they were incurred. Spire Missouri is not asking for recovery on flotation costs for the entire consolidated entity, but only as it applies to its own equity. This is not a suggestion that the capital structures of Spire Inc. and Spire Missouri are one in the same. Spire Missouri's capital structure is by definition part of the larger consolidated capital structure of Spire Inc. along with the capital contained within several other subsidiaries. This fact does not make the reverse true.

Q. IS OPC'S RECOMMENDED CAPITAL STRUCTURE AND RATE OF RETURN FAIR AND REASONABLE?

A. No. Mr. Murray's approach to capital structure and rate of return is deeply flawed and it would significantly impact Spire Missouri's ability to attract new capital at a reasonable cost. OPC has provided updated cost analysis in its True-up Testimony on all capital components except equity which is an inappropriate and suspicious omission given the obvious trends toward higher authorized ROEs as reported by Regulatory Research Associates[13]. Mr. Murray continues to cite the Empire electric proceeding as a "current" comparable ROE despite the financial analysis underlying the testimony in

[13] S&P Global Market Intelligence, RRA Regulatory Focus: Major Rate Case Decisions- January – June 2021, July 27, 2021.

that case stemming from 2019. OPC also offers an alternative capital structure based on a fundamentally flawed interpretation of rating agency methodology and continues to disagree with the Commission's long-held precedent excluding short-term debt from the capital structure and its customary "point in time" analysis.

The positions advocated by Mr. Murray should be familiar to the Commission. Very similar recommendations were made by him in the last Spire Missouri rate proceeding (while on the Commission's Staff)[14] and in subsequent rate proceeding since then. ** [redacted][15] **

Consistent application of the principles outlined in Spire Missouri's last rate proceedings to current circumstances should lead the Commission to once again reject Mr. Murray's recommendations.

V. RESPONSE TO STAFF'S TRUE-UP DIRECT TESTIMONY

[14] GR-2017-0215/GR-2017-0216, Staff's Cost of Service Report, pages 45-46; Murray Rebuttal Testimony.

[15] ** [redacted] **

Q. DID STAFF UPDATE ITS ROE RECOMMENDATION IN THE TRUE-UP DIRECT TESTIMONY OF KAREN LYONS?

A. No.

Q. SHOULD THE STAFF'S ROE NUMBER BE UPDATED?

A. Yes. Staff should update the ROE number based on the current information available to Staff, including information from recent utility cases which I included in my prior testimony.[16]

VI. CONCLUSION

Q. DOES THIS CONCLUDE YOUR TRUE-UP REBUTTAL TESTIMONY?

A. Yes.

[16] GR-2021-0108, Woodard Surrebuttal Testimony, Schedule AWW SR-1.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Spire Missouri Inc.'s Request for Authority to Implement a General Rate Increase for Natural Gas Service Provided in the Company's Missouri Service Areas	)))))	**File No. GR-2021-0108**

AFFIDAVIT

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

Adam Woodard, of lawful age, being first duly sworn, deposes and states:

1. My name is Adam Woodard. I am Treasurer for Spire Missouri Inc. My business address is 700 Market St., St Louis, Missouri, 63101.

2. Attached hereto and made a part hereof for all purposes is my testimony on behalf of Spire Missouri Inc.

3. Under penalty of perjury, I declare that the foregoing is true and correct to the best of my knowledge and belief.

/s/ Adam Woodard
Adam Woodard

August 16, 2021
Date