Exhibit No.:	
Issue(s):	*Rate of Return and Capital Structure*
Witness:	*Dave Murray, CFA*
Sponsoring Party:	*MoPSC Staff*
Type of Exhibit:	*Surrebuttal Testimony*
Case No.:	*WR-2018-0170*
Date Testimony Prepared:	*August 3, 2018*

MISSOURI PUBLIC SERVICE COMMISSION

COMMISSION STAFF DIVISION

FINANCIAL ANALYSIS DEPARTMENT

SURREBUTTAL TESTIMONY

OF

DAVID MURRAY, CFA

LIBERTY UTILITIES (MISSOURI WATER) LLC, d/b/a LIBERTY UTILITIES

CASE NO. WR-2018-0170

Jefferson City, Missouri
August 2018

SURREBUTTAL TESTIMONY

OF

DAVID MURRAY, CFA

LIBERTY UTILITIES (MISSOURI WATER) LLC,
d/b/a LIBERTY UTILITIES

CASE NO. WR-2018-0170

Q. What is your name?

A. My name is David Murray.

Q. Are you the same David Murray who sponsored the Rate of Return (ROR) used to establish the revenue requirement contained in Staff's Review and Audit of Liberty Utilities (Missouri Water) LLC, d/b/a Liberty Utilities (hereinafter referred to as "Liberty Water"), June 22, 2018 ("Staff Audit"), which was attached to Staff witness Paul R. Harrison's Direct Testimony filed as of the same date?

A. Yes.

Q. Are you the same David Murray who sponsored Rebuttal Testimony in this case?

A. Yes.

Q. What is the purpose of your Surrebuttal Testimony?

A. To respond to William G. Stannard's Rebuttal Testimony as it relates to a fair and reasonable ROE to authorize Liberty Water. Mr. Stannard sponsored testimony on behalf of Silverleaf Resorts Inc. and Orange Lake Country Club, Inc.

Q. What is Mr. Stannard's recommended allowed ROE in his Rebuttal Testimony?

A. Mr. Stannard identified a range of 8% to 9%.

Q. What is the basis for Mr. Stannard's recommendation?

A. Mr. Stannard adds Duff & Phelps' estimated equity risk premium of 5% to a spot 30-year Treasury yield of 2.97% to estimate a required return on common equity of approximately 8%. Mr. Stannard then adds 100 basis points to this base to allow for a range of 8% to 9%.

Q. Is Duff & Phelps an authoritative source as it relates to estimating the cost of capital?

A. Yes. Staff consistently relies on this source for purposes of testing the reasonableness of its own cost of equity estimates. Duff & Phelps publishes a comprehensive amount of data that assists financial analysts with estimating the cost of capital. Duff & Phelps assesses equity risk premium estimates derived using a variety of methods/sources/data, such as historical earned return spreads between stocks and bonds and implied equity risk premiums estimated by various authoritative sources, such as academics and investors.

Q. Does Mr. Stannard apply Duff & Phelps' suggested equity risk premium as Duff & Phelps' intends it to be applied?

A. No. Mr. Stannard applies the equity risk premium to a spot 30-year Treasury yield. Duff & Phelp's equity risk premium estimate is conditioned on a "normalized" risk-free rate of 3.5%. Adding the 5% conditional equity risk premium to this yield results in a market cost of equity of 8.5%.

Q. Did Mr. Stannard leave out a step to adjust the equity risk premium to reflect the fact that utility stocks are less volatile than the broader markets?

A. Yes. Utility stocks are less volatile than the broader market. This lower volatility is typically measured by calculating the beta of utility stocks. Typically, betas of utilities are in the range of 0.6 to 0.8. Applying a typical utility beta of 0.7 to the market risk premium of 5%, results in an industry adjusted risk premium of 3.5%. Adding this 3.5% adjusted risk premium to Duff & Phelp's normalized risk-free rate of 3.5% results in a cost of equity of 7%.

Q. If using authoritative sources in conjunction with widely-accepted cost of equity methods implies a cost of equity of 7%, why did you recommend a 10% allowed ROE for both Liberty Water and Liberty Midstates?

A. Because I am using the Commission's previous decisions as guidance as to a fair and reasonable allowed ROE, giving its most recent allowed ROE of 9.8% in the Spire Missouri gas rate cases, Case Nos. GR-2017-0216 and GR-2017-0217, the most weight. Being that Liberty Water has a more leveraged capital structure than that authorized Spire Missouri, Staff recommended a 20 basis point increase to the allowed ROE. Staff quantified the 20 basis point adjustment by evaluating recent spreads between 'BBB' rated bonds and 'A' rated bonds. For more detail, please see pages 47-48 of my "Detailed Direct Testimony" filed in the Liberty Midstates rate case.

Q. Does this conclude your Surrebuttal Testimony?

A. Yes.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In The Matter of the Application of Rate Increase for)
Liberty Utilities (Missouri Water), LLC d/b/a) **Case No. WR-2018-0170**
Liberty Utilities)

AFFIDAVIT OF DAVID MURRAY, CFA

State of Missouri)
) ss
County of Cole)

COMES NOW David Murray, CFA, and on his oath declares that he is of sound mind and lawful age; that he contributed to the foregoing *Surrebuttal Testimony*; and that the same is true and correct according to his best knowledge and belief. Further the Affiant sayeth not.

David Murray

David Murray, CFA

JURAT

Subscribed and sworn before me, a duly constituted and authorized Notary Public, in and for the County of Cole, State of Missouri, at my office in Jefferson City, on this 2nd day of August, 2018.

D. SUZIE MANKIN
Notary Public - Notary Seal
State of Missouri
Commissioned for Cole County
My Commission Expires: December 12, 2020
Commission Number: 12412070

D. Suzie Mankin

NOTARY PUBLIC