Exhibit No. 242

Commission Staff – Exhibit 242
Lisa M. Ferguson
Direct Testimony (Gas)
File Nos. ER-2021-0240 & GR-2021-0241

Exhibit No.:	
Issues:	*Report on Revenue Requirement Cost of Service, Overview of the Staff's Filing*
Witness:	*Lisa M. Ferguson*
Sponsoring Party:	*MoPSC Staff*
Type of Exhibit:	*Direct Testimony*
Case No.:	*GR-2021-0241*
Date Testimony Prepared:	*September 3, 2021*

MISSOURI PUBLIC SERVICE COMMISSION

COMMISSION STAFF

FINANCIAL & BUSINESS ANALYSIS DIVISION

AUDITING DEPARTMENT

DIRECT TESTIMONY

OF

LISA M. FERGUSON

UNION ELECTRIC COMPANY
d/b/a Ameren Missouri

CASE NO. GR-2021-0241

Jefferson City, Missouri
September 3, 2021

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OF

LISA M. FERGUSON

UNION ELECTRIC COMPANY
d/b/a AMEREN MISSOURI

CASE NO. GR-2021-0241

DIRECT TESTIMONY

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LISA M. FERGUSON

UNION ELECTRIC COMPANY,
d/b/a AMEREN MISSOURI

CASE NO. GR-2021-0241

Q. Please state your name and business address.

A. Lisa M. Ferguson, 111 North 7th Street, Suite 105, St. Louis, MO 63101.

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

A. I am employed by the Missouri Public Service Commission ("Commission" or "PSC") as a Utility Regulatory Supervisor.

Q. Please describe your educational background and work experience.

A. I attended Truman State University, receiving a Bachelor of Science degree and a Master's degree in Accounting in 2006 and 2008, respectively. Since joining the Commission's Staff in 2008, I have assisted with and directed audits and examinations of the books and records of utility companies operating within the state of Missouri.

Q. Have you previously filed testimony before this Commission?

A. Yes, I have. Please refer to Schedule 1, which is included in Staff's Appendix 1, for a list of cases in which I have previously filed testimony as well as the issues that I have addressed in testimony.

Q. What knowledge, skills, experience, training and education do you have in the areas of which you are testifying as an expert witness?

A. I have been employed by this Commission as a Utility Regulatory Auditor for over thirteen years and have submitted testimony on ratemaking issues numerous times before the Commission. I have also been responsible for the work product of other Commission employees in rate cases and other regulatory proceedings. Since the time I began my employment with the Commission, I have received training with regard to technical ratemaking matters both in-house and through attending National Association of Regulatory Utility Commissioners ("NARUC") sponsored regulatory seminars as well as other regulatory symposiums and conferences.

Q. Have you participated in the Commission Staff's audit of Union Electric Company, d/b/a Ameren Missouri ("Ameren Missouri" or "Company"), concerning its request for a rate increase in this proceeding?

A. Yes, I have, with the assistance of other members of the Staff. I am the Financial and Business Analysis Division case coordinator facilitating the work of Staff members within that Division, and I interface and work with the Staff members from other Commission Divisions and Departments that are involved in the Staff's direct case.

EXECUTIVE SUMMARY

Q. Please summarize your direct testimony in this proceeding.

A. I am sponsoring the Staff's Revenue Requirement Cost of Service Report ("Report") and Staff's Direct Accounting Schedules in this proceeding that are being filed concurrently with this direct testimony. I also provide in this direct testimony an overview of the Staff's revenue requirement determination. Staff has conducted a review of all the components (capital structure, return on rate base, rate base, operating revenues and operating expenses) that determine Ameren Missouri's revenue requirement. My testimony provides an overview of Staff's work in each area.

REVENUE REQUIREMENT COST OF SERVICE REPORT

Q. Please explain the organizational format of the Staff's Revenue Requirement Cost of Service Report.

A. The Staff's Report has been organized by topic as follows:

I. Executive Summary

II. Test Year/True-Up Period

III. Rate of Return (Capital Structure, Cost of Debt, Cost of Equity)

IV. Rate Base

V. Allocations

VI. Income Statement

VII. Depreciation

The Rate Base and Income Statement sections have numerous subsections which explain each specific area and/or adjustments made by the Staff to the test year ending December 31, 2020. The individual Staff member responsible for each area of Staff's direct case and/or adjustment is identified in the Report following the written discussion he or she authored, and is the expert/witness with respect to that section of the Staff's Report. The Staff may have a different or additional expert/witness for rebuttal or surrebuttal testimony in a given area if this case proceeds to evidentiary hearings.

OVERVIEW OF STAFF'S RECOMMENDED REVENUE REQUIREMENT

Q. How does one determine the revenue requirement for a regulated utility?

A. The first step is to calculate the utility's cost of service.

Q. In its audit of Ameren Missouri for Case No. GR-2021-0241, has Staff examined all of the components comprising the cost of service for Ameren Missouri's gas operations in Missouri?

A. Yes.

Q. What are the cost-of-service components that comprise the cost of service for a regulated, investor-owned public utility?

A. The cost of service for a regulated, investor-owned public utility can be defined by the following formula:

Cost of Service = Cost of Providing Utility Service

or

$$COS = O + (V - D)R \quad \text{where,}$$

COS = Cost of Service

O = Operating Costs (Fuel, Payroll, Maintenance, etc.), Depreciation and Taxes

V = Gross Valuation of Property Required for Providing Service (including plant and additions or subtractions of other rate base items)

D = Accumulated Depreciation Representing Recovery of Gross Depreciable Plant Investment

V – D = Rate Base (Gross Property Investment less Accumulated Depreciation = Net Property Investment)

(V – D)R = Return Allowed on Rate Base

In the past, the terms "cost of service" and "revenue requirement" have sometimes been used interchangeably. However, in this rate case, Staff will use the term "revenue requirement" to only refer to the utility's necessary incremental change in revenues based on measurement of the utility's current total cost of service compared to its current revenue levels under existing rates.

Q. What is the objective of an audit of a regulated, investor-owned public utility for ratemaking purposes?

A. The objective of an audit is to determine the appropriate level of the components identified in my previous answer in order to calculate the revenue requirement for such a regulated utility. All relevant factors are examined and a proper relationship of revenues, expenses, and rate base is maintained. The process for making that revenue requirement determination can be summarized as follows:

(1) <u>Selection of a test year.</u> The test year income statement represents the starting point for determining a utility's existing annual revenues, operating costs and net operating income. Net operating income represents the return on investment based upon existing rates. The test year approved by this Commission for Case No. GR-2021-0241, is the twelve months ending December 31, 2020. "Annualization," "normalization" and "disallowance" adjustments are made to the test year results when the unadjusted amounts do not fairly represent the utility's most current, ongoing and appropriate annual level of revenues and operating costs. Annualization, normalization and disallowance adjustments are explained in more detail later in this direct testimony.

(2) <u>Selection of a "test year update period."</u> A proper determination of revenue requirement is dependent upon matching the rate base, return on investment, revenues, and operating costs components at the same point in time. This ratemaking principle is commonly referred to as the "matching" principle. It is a standard practice in ratemaking in Missouri to utilize a period beyond the established test year in which to match the major

components of a utility's revenue requirement. By updating test year financial results to reflect information beyond the established test year, rates can be set based upon more current information. Due to the length of time between the end of the test year, December 31, 2020, and the true-up cutoff, September 30, 2021, no update period has been established in this case.

(3) Selection of a "true-up date" or "true-up period." A true-up date generally is established when a significant change in a utility's cost of service occurs after the end of the test year (or, if applicable, the end of the update period), but prior to the operation-of-law date, and the significant change in cost of service is one the parties and/or Commission has decided should be considered for cost-of-service recognition in the current case. The parties have agreed with a true-up cut-off date of September 30, 2021. The cost of these and other changes will be considered for inclusion in the cost of service during the true-up audit authorized by the Commission for this case.

(4) Determination of Rate of Return. A cost-of-capital analysis must be performed to allow Ameren Missouri the opportunity to earn a fair rate of return on its net investment ("rate base") used in the provision of utility service. Staff witness Seoung Joun Won, PhD of the Commission's Financial Analysis Department, has performed a cost-of-capital analysis and is sponsoring a section of the Staff's Revenue Requirement Cost of Service Report to explain and provide the results of his analysis.

(5) Determination of Rate Base. Rate base represents the utility's net investment used in providing utility service, on which the utility is permitted the opportunity to earn a return.

(6) Net Operating Income from Existing Rates. The starting point for determining net income from existing rates is the unadjusted operating revenues, expenses,

depreciation, and taxes for the test year which is the twelve-month period ending December 31, 2020, for this case. All of the utility's specific revenue and expense categories are examined to determine whether the unadjusted test year results require adjustments in order to fairly represent the utility's most current level of operating revenues and expenses. Numerous changes occur during the course of any year that will impact a utility's annual level of operating revenues and expenses. The December 31, 2020, test year has been adjusted to reflect the Staff's determination of the appropriate ongoing levels of revenues and expenses. These items will be re-examined based on actual data as part of the true-up process through September 30, 2021.

(7) Determination of Net Operating Income Required. The net income required for Ameren Missouri is calculated by multiplying the Staff's recommended rate of return by the rate base. Net income required is then compared to net income available from existing rates discussed in Item 6 above. The difference, when factored-up for income taxes, represents the incremental change in the utility's rate revenues required to cover its operating costs and to provide a fair return on investment used in providing gas service.

If a utility's current rates are insufficient to cover its operating costs and provide a fair return on investment, the comparison of net operating income required (Rate Base x Recommended Rate of Return) to net income available from existing rates (Operating Revenue less Operating Costs, Depreciation and Income Taxes) will result in a positive amount which would indicate that the utility requires a rate increase. If the comparison results in a negative amount, this indicates that the utility's current rates may be excessive.

Q. Please identify the types of adjustments which are made to unadjusted test year results in order to reflect a utility's current annual level of operating revenues and expenses.

A. The types of adjustments made to reflect a utility's current annual operating revenues and expenses are:

(1) Normalization adjustments. Utility rates are intended to reflect normal ongoing operations. A normalization adjustment is required when the test year reflects the impact of an abnormal event. One example of this type of adjustment that is made in all gas rate cases is the Staff's revenue adjustments to normalize weather. Actual weather conditions during the test year are compared to 30-year "normal" values. The weather normalization adjustment restates the test year sales volumes and revenue levels to reflect normal weather conditions.

(2) Annualization adjustments. Annualization adjustments are required when changes have occurred during the test year, update and/or true-up period, which are not fully reflected in the unadjusted test year results. For example, a portion of Ameren Missouri's employees received a wage increase on January 1, 2021. As a result, no part of the test year reflects the impact of this payroll increase. An adjustment was made to capture the financial impact of the payroll increase for the wage increase.

(3) Disallowance adjustments. Disallowance adjustments are made to eliminate costs in the test year results that are not considered prudent, reasonable, appropriate, and/or not of benefit to Missouri ratepayers and thus not appropriate for recovery from ratepayers. An example in this case is certain executive incentive compensation costs. In the Staff's view, these costs are incurred to primarily benefit shareholder interests and it is not appropriate policy to pass these costs on to customers in rates, since these costs do not benefit ratepayers. Therefore, these costs should be eliminated from the cost of service borne by ratepayers and the Staff has proposed to disallow these costs from recovery in rates.

(4) Pro forma adjustments. Pro forma adjustments reflect the impact of items and events that occur subsequent to the test year. These items or events significantly impact the revenue, expense and rate base relationship and should be recognized to address the forward-looking objective of the test year. Caution must be exercised when including pro forma adjustments in a recommended cost of service to ensure that all items and events subsequent to the test year are also examined and any appropriate offsetting adjustments are included as well. In addition, some post-test year items and events may not have occurred yet and/or may not be capable of adequate quantification at the time of the case filing. As a result, quantification of pro forma adjustments may be more difficult than the quantification of other adjustments. As a consequence, use of a true-up audit that considers a full range of auditable items and events that occur subsequent to the test year, attempts to address the maintenance of the proper relationship among revenues, expenses and investment at a consistent point in time is generally a superior approach than considering stand-alone pro forma adjustments for inclusion in cost of service.

Q. What rate increase amount, based on what return on equity ("ROE") percentage, did the Company request from the Commission in this case?

A. Ameren Missouri requested that its annual revenues be increased by approximately $9,403,160 based on an ROE of 9.80%.

Q. Please describe Staff's direct case revenue requirement filing in this proceeding.

A. The results of Staff's audit of Ameren Missouri's rate case request can be found in the Staff's filed Accounting Schedules and is summarized on Accounting Schedule 1, Revenue Requirement. This Accounting Schedule shows that the Staff's recommended revenue requirement for Ameren Missouri in this proceeding is $3,834,752 based upon a mid-point recommended rate of return ("ROR") of 6.725%. Staff is recommending a mid-point ROE of 9.50% with a range of 9.25% to 9.75% as calculated by Staff witness Dr. Seoung Joun Won, PhD. Staff's revenue requirement at low and high is $3,335,801 to $4,333,701 based upon a ROR range of 6.599% to 6.851%.

Q. What items are included in the Staff's recommended rate base in this case?

A. The rate base items include: Plant-in-Service, Accumulated Depreciation Reserve, Cash Working Capital, Materials and Supplies, Prepayments, Stored Gas Inventory, Customer Advances for Construction, Customer Deposits, Unamortized Pension and OPEBs Tracking Assets and Liabilities, and the Accumulated Deferred Income Tax ("ADIT") Reserve. The Plant and Depreciation Reserve balances reflect the Staff's estimates through the September 30, 2021, true-up cut-off date. Other rate base items reflect various levels at or beyond the end of the December 31, 2020, test year. These rate base components will be trued-up through September 30, 2021, once the true-up data becomes available.

Q. What are the significant income statement adjustments the Staff made in determining Ameren Missouri's revenue requirement for this case?

A. A summary of the Staff's significant income statement adjustments follows:

Operating Revenues

Retail revenues were adjusted for the elimination of unbilled revenue, PGA revenue, gross receipts taxes, customer growth, the update period, deliverability charge revenue and weather/days normalization.

Staff has also addressed a number of other issues in greater detail in the Staff's Revenue Requirement Cost of Service Report as shown in the partial listing below:

Payroll, Payroll Taxes and Employee Benefit Costs

- Payroll expense annualized for all known wage increases through January 1, 2021, and changes in employee levels through June 30, 2021.
- Payroll taxes consistent with the payroll annualization and incentive compensation removals.
- Incentive compensation and restricted stock awards disallowances.
- Employee benefits including pensions and OPEBs.

Other Non-Labor Expenses

- Customer Convenience Fees
- Distribution Maintenance Expense
- Rents and Leases
- Insurance Expense
- Property Tax Expense
- Uncollectible Expense
- Corporate Allocations
- Rate case expense adjustment.
- Disallowance of all institutional advertising expense, certain dues and donations and miscellaneous expenses and Ameren Corporation board of directors related costs.
- Income Taxes
- Depreciation Expense

Q. What reliance did you place on the work or conclusions of other Staff members working on Staff's behalf?

A. All of the Staff auditors, including myself, relied on the work from numerous other Staff members in calculating a revenue requirement for Ameren Missouri in this case. Weather-normalized sales, depreciation rates and the recommended rate of return are some examples of data and analysis supplied to the Auditing Unit as inputs into the Staff's revenue requirement cost-of-service calculation. Signed affidavits and the qualifications for all Staff members who are responsible for a section of the Staff's Revenue Requirement Cost-of-Service Report and for whom that section constitutes direct testimony in this rate proceeding are attached in an appendix to the Report. Each Staff member who is responsible for a section of the Staff's Revenue Requirement Cost-of-Service Report is identified at the conclusion of the section he or she authored as being the Staff expert/witness responsible for that section.

Q. What are the biggest differences between the rate increase request filed by the Company and the Staff revenue requirement recommendations being filed in this proceeding?

A. From the Staff's perspective, there are five primary revenue requirement differences.

- Return on Equity (ROE) and Capital Structure – Issue Value – ($1.2 million). As previously stated, Ameren Missouri's return on equity recommendation is 9.80%, while the Staff has developed a mid-point recommendation of 9.50%. The dollar difference between Ameren Missouri's recommended ROE and Staff's recommended mid-point for ROE, 9.80% compared to 9.50%, is approximately $1.2 million in revenue requirement.
- Payroll – Issue Value – ($0.7 million). Staff has included Ameren Missouri's employee headcount as of June 30, 2021. Ameren Missouri included temporary employees in its headcount through September 30, 2021 in its direct filed revenue requirement for which the actual headcount increase Staff has included only permanent employees as of June 30, 2021.
- Low Income Weatherization – Issue Value – ($0.7 million). Ameren Missouri has erroneously included this amount twice in its direct revenue requirement.

Once in the operations & maintenance account and again in amortization expense.

- Incentive Compensation - Issue Value ($0.25 million). Ameren Missouri has included a level of earnings based incentive compensation in its direct case for which Staff has removed.

- Employee Benefits – Issue Value ($0.12 million). Staff has included Ameren Missouri's employee headcount as of June 30, 2021. Ameren Missouri included temporary employees in its headcount through September 30, 2021 in its direct filed revenue requirement for which the actual headcount increase Staff has included only permanent employees as of June 30, 2021.

There are other significant differences between the Staff and the Company, based upon their respective direct filings. However, these items are less significant than the differences discussed above.

Q. Is it possible that significant differences exist between the Staff's revenue requirement positions and those of other parties besides Ameren Missouri in this proceeding?

A. Yes. However, the other parties are filing their prepared direct testimony, if any, concurrently with the Staff's direct filing. Until Staff has a chance to examine the direct testimony of the other parties, it is impossible for the Staff to determine what differences exist and how material they may be.

Q. Please identify the Staff experts/witnesses responsible for addressing each area where there is a known and significant difference between Staff and Ameren Missouri as addressed above in this direct testimony.

A. The Staff experts/witnesses for each listed issue are as follows:

Issue	Staff Witness
Rate of Return	Seoung Joun Won, PhD
Payroll	Paul K. Amenthor
Low Income/Weatherization Amortization	Jason Kunst, CPA
Incentive Compensation	Jason Kunst, CPA
Employee Benefits	Paul K. Amenthor

Q. When will the Staff be filing its customer class cost of service and rate design direct testimony and report in this proceeding?

A. Staff's customer class cost of service and rate design direct testimony and report and schedules will be filed on September 17, 2021.

Q. Does this conclude your prepared direct testimony in this proceeding?

A. Yes, it does.