Exhibit No.:	________________
Issue(s):	Rate of Return/Capital Structure
Witness/Type of Exhibit:	Murray/Surrebuttal True-Up Direct
Sponsoring Party:	Public Counsel
Case No.:	GR-2024-0369

SURREBUTTAL/TRUE-UP DIRECT

TESTIMONY

OF

DAVID MURRAY

Submitted on Behalf of the Office of the Public Counsel

UNION ELECTRIC COMPANY
D/B/A AMEREN MISSOURI

FILE NO. GR-2024-0369

** **
Denotes Confidential Information that has been redacted

May 2, 2025

PUBLIC

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SURREBUTTAL/TRUE-UP DIRECT TESTIMONY

OF

DAVID MURRAY

UNION ELECTRIC COMPANY d/b/a AMEREN MISSOURI

FILE NO. GR-2024-0369

Q. Please state your name and business address.

A. My name is David Murray and my business address is P.O. Box 2230, Jefferson City, Missouri 65102.

Q. Are you the same David Murray who previously filed Direct and Rebuttal Testimony in this case?

A. Yes.

Q. What is the purpose of your testimony?

A. My testimony will respond to Ameren Missouri witnesses Darryl T. Sagel's and Ann E. Bulkley's rebuttal testimonies as they relate to rate of return ("ROR") and capital structure. I also address the rebuttal testimony of Staff witness Seoung Joun Won, PhD.

Additionally, I will update my ROR recommendation to consider Ameren Corp's and Ameren Missouri's financial activities through the ordered true-up date in this case, December 31, 2024.

Q. In what order will you address these issues/witnesses?

A. First, I will update my ROR recommendation based on financial data through the true-up date. Second, I will address capital structure, which was the sole ROR issue addressed by Mr. Sagel. Dr. Won also disagrees with the premise of using Ameren Corp as a proxy for a fair and reasonable ratemaking capital structure for Ameren Missouri. Finally, I will address Ms. Bulkley's response to my recommended allowed ROE of 9.50% for Ameren Missouri's natural gas distribution utility operations.

TRUE-UP RECOMMENDATION

Q. Are you able to provide an updated recommended ROR as of the December 31, 2024, true-up date?

A. Yes. While I am not changing my recommended ratemaking capital structure, I am updating Ameren Missouri's cost of long-term debt to 4.296% from 4.12%. The increase in Ameren Missouri's embedded cost of long-term debt was caused by Ameren Missouri's two long-term debt issuances between the test year and true-up period. Specifically, Ameren Missouri issued $500 million of long-term debt on April 4, 2024, at a 5.2% coupon rate, and issued $450 million of long-term debt on October 7, 2024, at a 5.125% coupon rate.

Q. What is your recommended ROR as of the true-up date?

A. 6.48%. Please see Schedule DM-S-1 for the details related to my recommended ROR as of the true-up date.

CAPITAL STRUCTURE

Q. Summarily, how does your assessment of the appropriate ratemaking capital structure to set Ameren Missouri's authorized ROR for its natural gas distribution operations differ from the other witnesses?

A. My recommended ratemaking capital structure considers Ameren Corp's utilization of a higher proportion of debt in its consolidated capital structure as compared to Ameren Missouri's per books capital structure. The other witnesses support the use of Ameren Missouri's per books capital structure.[1] They both assert that this capital structure is appropriate for ratemaking because, in their view, it is independently managed for its own benefit, and, presumably, for the benefit of Ameren Missouri's ratepayers. While I agree that Ameren Missouri's capital structure is carefully managed, it is managed for one primary purpose—achieving a constant 52% authorized equity ratio regardless of changes

[1] Mr. Sagel's and Dr. Won's preferred stock and long-term debt balances are adjusted slightly for premiums, discounts and issuance expenses to arrive at a carrying value/net proceeds balance, but their capital structure recommendations are premised on Ameren Missouri's balance sheet ratios, not Ameren Corp's balance sheet ratios.

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in business and economic conditions. Ameren Missouri's common equity ratio has been maintained at 52% for ratemaking, despite declining business risk since 2018, but Ameren Corp's common equity ratio has consistently declined during the same period. This fact alone should elicit enhanced scrutiny.

Ameren Missouri's equity ratio hasn't budged from the 52% target over the last twelve years despite its reduced business risk due to the passage of utility-favorable legislation in Missouri. The 2018 legislation enabling plant-in-service accounting ("PISA") prompted Ameren Corp to dramatically increase the amount and growth of its investment in Ameren Missouri. In 2022, the Missouri legislature amended the PISA law to allow electric utility companies to continue to utilize PISA through at least 2028. Another utility-favorable statute is the 2022 law allowing Missouri utility companies the ability to securitize both undepreciated balances of fossil-fuel plants retired early and extraordinary costs such as those incurred during extraordinary weather events. It would be less egregious for ratepayers to pay the higher cost of capital associated with a 52% equity ratio if Ameren Corp targeted this more conservative level for itself as well. Instead, Ameren Corp's common equity ratio has declined to the low 40% range in recent years.

Q. So, you believe that Ameren Corp's financial interests play a role in the financial management of Ameren Missouri?

A. I do. I will show that Ameren Missouri's capital structure has not been managed for its or its ratepayers' best interests. Ameren Missouri's ratepayers are paying for the costs of more shareholder-friendly ratemaking mechanisms, but not receiving the benefit of the lower-cost capital structure these mechanisms allow (*i.e.* higher debt capacity).

INCREASED DEBT CAPACITY FROM LOWER BUSINESS RISK

Q. Does Mr. Sagel recognize that Ameren Corp's debt capacity has increased since Ameren Missouri received the benefit of PISA?

A. Yes, but it is his position that Ameren Missouri's election of PISA is only one factor Moody's considered when it lowered Ameren Corp's funds-from-operations-to-debt

("FFO/debt")[2] downgrade threshold to 17% from 19%. Mr. Sagel indicates Ameren Corp's increased debt capacity was also due to "a strong track record of strategy execution within the then-supportive regulatory frameworks of Ameren Corporation's Ameren Illinois Corporation ("AIC") and Ameren Transmission Company of Illinois ("ATXI") subsidiaries."[3]

Q. Did Moody's lower its FFO/debt downgrade threshold for AIC or ATXI?

A. Not to my knowledge.

Q. Is it logical for the operating subsidiaries, which directly own the assets, not to have increased debt capacity due to supportive regulatory frameworks?

A. No.

Q. Then why would Moody's lower its downgrade threshold for Ameren Corp rather than its downgrade thresholds for Ameren Missouri, AIC, and ATXI?

A. As I will explain in more detail later in my testimony, when interacting with the rating agencies, the officers representing Ameren Corp and its subsidiaries are primarily acting as fiduciaries for Ameren Corp rather than each of Ameren Corp's subsidiaries, including Ameren Missouri.

Q. Why would those managing Ameren Corp and its subsidiaries only lobby to relax Ameren Corp's credit metrics rather than those used for its subsidiaries?

A. Because, lowering Ameren Corp's cost of capital, while maintaining its subsidiaries' higher common equity ratios for ratemaking, increases Ameren Corp's shareholders' wealth.

[2] Although there are subtle differences between Moody's cash flow from operations before working capital divided by debt ("CFO Pre-WC/Debt") ratio and an FFO/debt ratio, I will generally refer to Moody's CFO Pre-WC/Debt ratio as "FFO/debt," which is similar to Mr. Sagel's reference to such in his rebuttal testimony.
[3] Sagel Rebuttal, p. 23, lns. 11-16.

Q. Mr. Sagel testifies that Moody's rejected Ameren Corp's management's argument to ** [redacted] **[4] **Is he correct?**

A. No. ** [redacted] **

Q. Has Ameren Corp taken advantage of this lower downgrade threshold in its financing strategies?

A. Yes. Since 2019, Ameren Corp has approximately tripled the percentage of holding company debt it uses to finance its subsidiaries (8.39% at June 30, 2019 compared to 23.39% at March 31, 2024).[5]

Q. Has Ameren Missouri lowered its requested ratemaking common equity ratio over this period to recognize the additional debt capacity it supports?

A. No.

[4] *Id.,* p. 23, ln. 17 – p. 24, ln. 1.
[5] Murray Direct, p. 39, lns. 8-16.

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FIDUCIARY/CONFLICTS OF INTEREST

Q. Do officers and directors of Ameren Corp's family of companies serve in multiple and revolving functions/positions?

A. Yes.

Q. What is Mr. Sagel's position with Ameren Missouri?

A. He is Vice President and Treasurer.

Q. What are Mr. Sagel's positions at Ameren Corp, AIC, and ATXI?

A. He is Vice President and Treasurer at each company.

Q. Does Mr. Sagel holding the same financial-management positions at each of these affiliates raise concerns?

A. Yes. Specifically, it raises concerns as to his willingness to bargain for the financial interests of each of these entities at the same time. The fact that Mr. Sagel seems to simply accept that Ameren Missouri had not received any credit for its reduced business risk profile is disturbing. It certainly illustrates that Ameren Missouri is not bargaining for its financial interests and the interests of its customers, even if Ameren Missouri does have its own board of directors ("BOD") and officers. If the interests of Ameren Missouri and its ratepayers were being protected, then its officers would have bargained for Ameren Missouri's rightful debt capacity. Ameren Missouri's BOD's and officers' indifference is even more concerning given that, before 2019, Ameren Missouri's cash flows and dividends supported Ameren Corp's ability to finance investments in its other subsidiaries.

Q. What evidence do you have that Ameren Missouri's officers have not bargained for Ameren Missouri's financial interests?

A. Ameren Corp's December 17, 2018, presentation to Moody's (Schedule DM-S-2) clearly shows that ** ____________________

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Q. How do you know it is Ameren Missouri's reduced business risk that caused Moody's to lower its FFO/debt threshold for Ameren Corp?

A. Because Ameren Corp's management effectively said as much. During Ameren Corp's Finance Committee Meeting on February 7, 2019, Ameren Corp management stated:

> ** **[6]

Ameren Corp management also stated the following during Ameren Corp's Financing Committee Meeting on May 2, 2019:

> ** **[7]

Q. Did Ameren Missouri lobby Moody's for a lower FFO/debt threshold for purposes of the credit rating Moody's assigns to Ameren Missouri's debt?

A. No. I found no evidence of either Ameren Corp or Ameren Missouri presenting an analysis to Moody's comparing Ameren Missouri's FFO/debt metrics to those of its peers.

Q. Who presented information to the rating agencies on behalf of Ameren Corp, Ameren Missouri, and AIC?

A. According to a December 2018 rating agency presentation, Marty Lyons, Bruce Steinke and Darryl Sagel made the presentation.

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[6] Ameren Corp's Finance Committee Meeting, February 7, 2019, p. 24.
[7] Ameren Corp's Finance Committee Meeting, May 2, 2019, p. 87

Q. Were they officers of Ameren Corp at the time?

A. Yes. Marty Lyons was Executive Vice President and Chief Financial Officer; Bruce Steinke was Senior Vice President, Finance and Chief Accounting Officer; and Darryl Sagel was Vice President and Treasurer.

Q. Did they have the same positions at Ameren Missouri and AIC at that time?

A. Yes.

Q. Were they employees of Ameren Corp, Ameren Missouri, or AIC at the time?

A. No. Ameren Services Corporation employed each of these individuals.

Q. Were any officers solely representing Ameren Missouri for purposes of the rating agency presentation?

A. No.

Q. With regard to Ameren Missouri's ratemaking capital structure in this case, what do you conclude from the foregoing information?

A. The Commission is the only entity with the authority to ensure Ameren Missouri's ratepayers are given due consideration for their contribution to Ameren Missouri's lower business risk. The Commission can objectively provide Ameren Missouri's ratepayers their due consideration by setting Ameren Missouri's ratemaking common equity ratio consistent with that of Ameren Corp on a consolidated basis.

Mr. Sagel acknowledges that Ameren Missouri's ability to elect PISA was at least the tipping point for Ameren Corp being allowed a more leveraged profile. However, in Ameren Missouri's last several rate cases, he has stood firm in his refusal to give Ameren Missouri's customers any consideration in the form of a more leveraged and cost-efficient capital structure. In my opinion, this is one of the clearest examples of the need for the Commission to assert its authority to ensure a fair and reasonable outcome for ratepayers. Otherwise, Ameren Corp's shareholders are unfairly enriched by way of Ameren Missouri's ratepayer-supported debt capacity.

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Q. What Stand-Alone Credit Profile ("SACP") had S&P assigned to Ameren Missouri in the past?

A. Until September 2019, S&P assigned Ameren Missouri a SACP of an 'A-', but it was ultimately assigned a 'BBB+' issuer credit rating due to its affiliation with Ameren Corp.

Q. Why did S&P assign Ameren Missouri a stronger SACP?

A. Primarily because Ameren Missouri's financial risk profile ("FRP"), e.g. higher FFO/debt ratios, is healthier. However, because Ameren Corp's FRP was weaker, Ameren Missouri's S&P credit rating was limited to a 'BBB+'.

Q. Has Ameren Missouri's stronger FRP provided credit support to Ameren Corp when Ameren Corp provided financial support for investments in ATXI and AIC in the past?

A. Yes. From 2014 to 2017, Ameren Corp directly supported investment in ATXI by issuing debt to fund equity capital contributions and loans to ATXI. Ameren Corp indirectly supported investment in AIC for much of the past decade by allowing it to retain up to 100% of its net income, rather than paying dividends to Ameren Corp. From the period 2011 until 2018, Ameren Missouri's annual dividend payout ratio (net of capital contributions) to Ameren Corp was in the range of 87.22% in 2016 to 148.28% in 2011, with an average payout ratio of 105.22% over this period.

Additionally, during this time frame, Ameren Missouri's FFO/debt ratios were typically in the range of 24% to 27%—significantly higher than the 19% FFO/debt threshold required to maintain a 'Baa1' credit rating. Ameren Missouri could have issued more debt during this period and still had a comfortable FFO/debt margin above 19%. However, if Ameren Missouri issued that debt, it would have caused Ameren Corp's consolidated FFO/debt ratio to be lower. It was important for Ameren Corp to maintain a higher FFO/debt ratio over this period to ensure it could raise economically priced debt capital to fund significant investment in ATXI. After Ameren Corp accumulated a significant amount of short-term debt to fund investment in ATXI and refinance $425 million of long-term debt, Ameren Corp issued $700 million of bonds in 2015. Ameren Missouri's FFO/debt ratio of 26.7%

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in 2015[8] supported Ameren Corp's consolidated FFO/debt ratio of 24.4% during the same year.[9] Ameren Corp's healthy FFO/debt ratios allowed it to raise reasonably priced debt capital.

Q. Have Ameren Corp's business and financial risks impaired Ameren Missouri's financing flexibility in the past?

A. Yes. Ameren Missouri was foreclosed access to commercial paper markets in August 2008 due to the downgrade of its Moody's short-term credit rating to P-3, which occurred in conjunction with Moody's downgrade of Ameren Corp's long-term credit rating to 'Baa3'. This downgrade was primarily caused by financial difficulties at Ameren Missouri's affiliates.

Ameren Corp's S&P credit rating at the time was 'BBB-', which meant Ameren Missouri was also rated 'BBB-'. S&P downgraded Ameren Corp's and Ameren Missouri's credit ratings to 'BBB-' on April 23, 2007, due to negative developments related to Ameren Corp's Illinois' subsidiaries. S&P's ratings guidelines also dictate a lower short-term rating of A-3 if a company is assigned the lowest notch of long-term investment grade credit ratings.

S&P's and Moody's Tier-3 short-term ratings foreclosed Ameren Missouri's access to short-term credit markets, which proved to be quite costly to Ameren Missouri's ratepayers because of liquidity concerns. Ameren Missouri's ratepayers were charged for carrying costs due to the delay in installing scrubbers at Ameren Missouri's Sioux Energy Center.

Q. Why do you conclude that these downgrades foreclosed Ameren Missouri's ability to access commercial paper?

A. Because Evergy Metro (f/k/a Kansas City Power & Light Company) had at least one Tier-2 rating, which allowed it to continue to issue commercial paper to fund its Iatan 2 plant construction during the period of the financial crisis in 2008 to 2009.

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[8] Moody's Credit Opinion, Union Electric Company, March 29, 2019, Exhibit 2, p. 2.
[9] Moody's Credit Opinion, Ameren Corporation, March 29, 2019, Exhibit 2, p. 2.

Q. Why are circumstances from fifteen years ago relevant to this case?

A. I am illustrating the hypocrisy of Mr. Sagel's expressed concerns about Ameren Missouri's ratepayers paying a higher ROR to provide financial stability for a parent company that hasn't always reciprocated. If Ameren Corp desires Ameren Missouri's ratemaking equity ratio to be set at 52%, then Ameren Corp should issue more equity and less debt to achieve an equity ratio more consistent with the 52% it apparently considers important for financial flexibility.

OTHER MISSOURI UTILITY COMPANIES' FINANCIAL RISK PROFILES

Q. Are you aware of other Missouri utilities the Commission should consider when evaluating Ameren Corp's argument that Ameren Missouri's assets cannot support more debt and lower FFO/debt ratios and still maintain its credit rating?

A. Yes. The Commission should consider the ratings treatment afforded to Missouri's other major electric utility companies, Evergy Metro and Evergy Missouri West.

Q. What is Evergy Metro's current Moody's rating?

A 'Baa1,' which is the same as Ameren Missouri's.

Q. Mr. Sagel testifies that in its May 13, 2024, credit opinion on Ameren Missouri, Moody's lowered the FFO/debt downgrade threshold to 18% from the 19% it had consistently identified in credit opinions published on Ameren Missouri since at least 2019. Did Mr. Sagel explain Moody's rationale for lowering Ameren Missouri's FFO/debt downgrade threshold?

A. No. Mr. Sagel testified that the May 13, 2024, Moody's credit opinion did not provide a specific discussion regarding Moody's rationale for lowering the FFO/debt downgrade threshold. Mr. Sagel explained that Ameren Missouri's FFO/debt ratios had been at or below the previous 19% threshold for three of the four years between 2020 to 2023 so "it appears that Moody's is now willing to give the Company a bit more flexibility on this metric prospectively…"[10]

Q. Are you surprised Mr. Sagel is speculating as to why Moody's lowered Ameren Missouri's FFO/debt downgrade threshold to 18% from 19%?

A. Yes. Considering Mr. Sagel is part of Ameren Corp's team that interacts with and makes presentations to the credit rating agencies, I would expect him to be able to provide more than a speculative explanation for Moody's decision to loosen the FFO/debt threshold for Ameren Missouri. However, his testimony is consistent with Ameren Corp's priority of lobbying for less restrictive credit metric thresholds for Ameren Corp rather than Ameren Missouri.

Q. What is your view of the potential reason for Moody's decision to lower its FFO/debt downgrade threshold for Ameren Missouri?

A. Moody's recognized it was inconsistent in requiring a higher FFO/debt threshold for Ameren Missouri as compared to Evergy Metro. I have testified in Ameren Missouri rate cases since at least 2021 about Moody's inconsistent lower threshold of 18% for Evergy Metro as compared to 19% for Ameren Missouri.

Mr. Sagel's apparent lack of first-hand knowledge as to what caused Moody's to eventually lower the FFO/debt threshold for Ameren Missouri further demonstrates that neither Mr. Sagel nor any other Ameren Missouri officer has bargained for Ameren Missouri's interests. It appears that Missouri's utility regulators, through critical analysis of Moody's practices, are the primary stakeholder attempting to ensure Ameren Missouri's ratepayers are given due consideration for Ameren Missouri's lower business risk.

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[10] Sagel Rebuttal, p. 22, lns. 11-19.

Q. When Ameren Corp's officers lobbied Moody's to lower its FFO/debt thresholds for Ameren Corp, did they perform a comparative analysis of Ameren Corp's FFO/debt ratios to that of other companies?

A. Yes. As shown on pages 18 and 19 of Schedule DM-S-2, when Ameren Corp's officers lobbied Moody's to lower its FFO/debt threshold, it compared Moody's downgrade threshold of its peer utility holding companies to itself.

Q. Has Ameren Corp ever provided a similar analysis for Ameren Missouri, highlighting Moody's inconsistent FFO/debt thresholds for Evergy Metro and Ameren Missouri?

A. Not that I am aware of. I have reviewed all of Ameren Corp's rating agency presentations since 2019. I did not find evidence of a similar presentation performed on behalf of Ameren Missouri. If Ameren Corp had conducted such analysis on behalf of Ameren Missouri, Mr. Sagel would be able to testify first-hand that this was the rationale for Moody's lowering Ameren Missouri's FFO/debt threshold to 18%.

Q. What was Evergy Metro's last authorized capital structure for purposes of setting its allowed ROR?

A. In Evergy Metro's (f/k/a Kansas City Power & Light Company) last fully litigated rate case, Case No. ER-2016-0285, the Commission authorized Evergy Metro a ratemaking capital structure consisting of 49.2% common equity and 50.8% long-term debt.

Q. Did any rating agencies place Evergy Metro on a "negative watch" or "negative outlook" after the Commission authorized that capital structure?

A. No.

Q. Did Evergy Metro recommend an equity ratio similar to that which the Commission authorized?

A. Yes. Evergy Metro recommended a common equity ratio of 49.72%.

Q. What ratemaking capital structure did Evergy Missouri West request in its recent rate case, Case No. ER-2024-0189?

A. Evergy Missouri West ("EMW") initially requested its authorized ROR be premised on a capital structure expected to consist of 52.04% common equity as of the true-up date, June 30, 2024[11]

Q. Did Evergy Inc. manage its inter-company capital flows to achieve its initial requested common equity ratio of approximately 52%?

A. No. Instead of managing its inter-company capital flows to achieve a 52% common equity ratio, Evergy Inc. managed EMW's capital flows to achieve a 49.88% common equity ratio as of the true-up date.

Q. Could Evergy Inc. easily have achieved its initial requested ratemaking common equity ratio of 52% for EMW?

A. Yes.

Q. How did Evergy Inc. initially plan to achieve a 52% projected ratemaking common equity ratio for EMW?

A. EMW's witness Kirkland B. Andrews testified that EMW planned to issue $200 million of long-term debt before June 30, 2024, and retain a projected amount of income classified as confidential in the case. While EMW fell slightly short on the projected amount of retained earnings from income, the major driver causing EMW's common equity ratio to be approximately 50% was its decision to issue $300 million of long-term debt rather than $200 million.

[11] Case No. ER-2024-0189, Direct Testimony of Kirkland B. Andrews, p. 4, lns. 2-6.

Q. Did EMW recommend the use of the 49.88% common equity ratio to set is authorized ROR?

A. Yes. EMW agreed that its authorized ROR should be set based on this common equity ratio.[12]

Q. Are you aware of a negative reaction from the investment community because EMW decided to adjust its ratemaking capital structure to an approximate 50% common equity ratio?

A. No.

Q. What were EMW's FFO/debt ratios in 2022 and 2023, respectively?

A. 15.4% and 9.8%.[13]

Q. What did Moody's project them to be over the next two-to-three years?

A. 12% to 14%.[14]

Q. If Ameren Missouri had managed its internal capital flows to achieve a common equity ratio of no higher than 50% at the true-up date in this case, would you expect a negative reaction from rating agencies?

A. No. It is common for utility regulatory jurisdictions to set authorized common equity ratios at approximately 50%. Unfortunately, when utility companies communicate to investors that they expect a higher authorized common equity ratio, consistent with their recommendations, this communication causes investors to value the stock based on the company's optimistic guidance. If the stock price of a utility company's publicly-traded parent company declines after a commission authorizes a more reasonable common equity ratio, it does not necessarily imply that investors expect more risk going forward, it just reflects a reset in the level of expected earnings.

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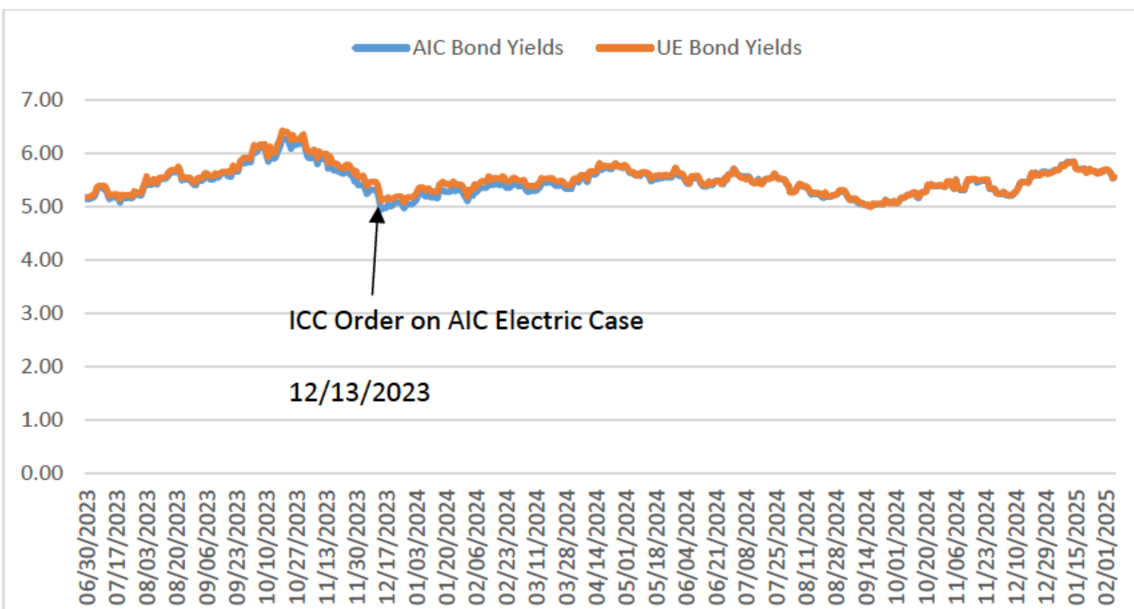
[12] *Id.,* Ronald A. Klote True-up Rebuttal Testimony, p. 7, lns. 5-14.
[13] Moody's Credit Opinion, Evergy Missouri West, May 9, 2024, p. 2.
[14] *Id.,* p. 1.

Q. Can you provide an example?

A. Yes. Ameren Corp is the perfect example because of the recent decision by the Illinois Commerce Commission ("ICC") that authorized a lower ROE than investors expected, which was applied to a 50% authorized common equity ratio. Although Ameren Corp's stock price declined after the ICC's decision, going forward investors recognized that the recovery of the lower adjusted level of capital expenditures is still highly probable.

This reality has also been recognized by debt investors in AIC's outstanding debt. The yield-to-maturity ("YTM") on AIC's debt has not been more costly than the YTM on Ameren Missouri's debt. In fact, the YTM on AIC's debt has even been slightly lower than similar maturities for Ameren Missouri debt. The following chart, comparing AIC and Ameren Missouri debt issuances with similar terms,[15] shows how closely these bonds have traded since before and after the ICC's decision on AIC's multi-year rate case on December 13, 2023:



[15] AIC yields are based on bonds with the following CUSIP identifiers: 02361DAT7, 02361DAU4, 02361DAX8, and 02361DAZ3. Ameren Missouri yields are based on bonds with the following CUSIP identifiers: 906548CQ3, 906548CS9, 906548CU4 and 906548CW0.

COMPARISON TO AMEREN ILLINOIS' CAPITAL STRUCTURE ARGUMENTS BEFORE THE ILLINOIS COMMERCE COMMISSION

Q. Mr. Sagel warns of potential negative credit and cost of capital ramifications if the Commission were to authorize Ameren Missouri a lower common equity ratio than that shown on Ameren Missouri's books.[16] Have any other Ameren Corp subsidiaries raised similar warnings in the past?

A. Yes. AIC witnesses raise the same warning to argue for a higher authorized common equity ratio for purposes of implementing its electric utility rates after it was allowed to use formula rates starting in 2012.

Q. What happened in that situation?

A. After Illinois' passage of the Energy Infrastructure Modernization Act ("EIMA") in 2011, AIC began filing annual rate cases for its electric utility in Illinois. Over the course of approximately three years, AIC and ICC Staff vigorously debated a fair and reasonable ratemaking common equity ratio in which to apply the formula ROE of 580 basis points plus a 12-month average 30-year United States Treasury yield. The arguments in the AIC rate cases were quite similar to those Ameren Missouri has made in its last few rate cases in Missouri. AIC's witnesses asserted AIC had to maintain a higher common equity ratio to offset higher business risks associated with the Illinois regulatory environment.[17]

Q. What ratemaking common equity ratio did AIC recommend in the inaugural case (2012) pursuant to Illinois' Energy Infrastructure Modernization Act?

A. 54.297% in Docket No. 12-0001.[18]

Q. What equity ratio did the ICC Staff witness recommend in that case?

A. 51.49%.

[16] Sagel Rebuttal, p. 26, lns. 1-14.
[17] Illinois Docket No. 12-001, Ryan J. Martin Rebuttal Testimony, p. 5, l. 97 through p. 6, l. 116.
[18] Illinois Docket No. 12-0001, Schedule D-1 Sponsored by Ryan J. Martin

Q. What common equity ratio did the ICC authorize?

A. 51.49%.

Q. What common equity ratio did AIC recommend for its electric utilities in its 2013 rate case, Docket No. 13-0301?

A. 54.62%.

Q. What common equity ratio did the ICC Staff recommend?

A. 51%.

Q. What was the premise for ICC Staff's recommended common equity ratio in AIC's 2013 rate case?

A. Ameren Corp's average consolidated common equity ratio for 2011.

Q. What common equity ratio did the ICC authorize in that case?

A. 51%.

Q. What common equity ratio did AIC recommend for its electric utilities in its 2014 rate case, Docket No. 14-0317?

A. 51%.

Q. What about the ICC Staff?

A. 51%.

Q. Why did the ICC Staff recommend the same common equity ratio in AIC's 2014 rate case?

A. Because the ICC Staff and AIC had agreed to use a 51% common equity ratio for purposes of that case.

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Q. Did the ICC adopt the 51% common equity ratio recommended by AIC and ICC Staff?

A. Yes.

Q. Did they agree to use that same equity ratio in subsequent cases?

A. No. They agreed to use a 50% common equity ratio, which was later codified as an amendment to the EIMA.

Q. Over the period of these cases in which AIC's fair and reasonable ratemaking capital structure was debated and decided by the ICC, were AIC's credit ratings put on a negative outlook or watch?

A. No.

Q. Can you briefly discuss the differing capital structure positions in AIC's recent multi-year rate plan case at the ICC?

A. Yes. AIC witness Daryl Sagel recommended the ICC authorize common equity ratios between 53.973% and 54.031% for the four years of the multi-year plan (2024 to 2027).[19] ICC Staff witness Janis Freetly, recommended the ICC authorize a ratemaking common equity ratio of 50% based on the statutory guidance that a 50% common equity ratio would be deemed reasonable unless AIC provided compelling evidence that a higher common equity ratio is needed for ratemaking.[20] Christopher Walters, witness for the Illinois Industrial Energy Consumers, the Federal Executive Agencies, the Citizens Utility Board, the United Congregations of Metro-East and Prairie Rivers Network, recommended the ICC authorize AIC a ratemaking common equity ratio of 50%. Mr. Walters' recommended common equity ratio was also premised on the fact that AIC's authorized ROR had been premised on the statutory guidance that a 50% common equity ratio had been deemed reasonable in AIC's formula rate plan cases.[21]

[19] ICC Docket Nos. 22-0487 and 23-0082, Darryl T. Sagel Direct Testimony, p. 3. Table 1.
[20] *Id.,* Janis Freetly Direct Testimony, p. 6, lns. 104-115.
[21] *Id.,* Christopher C. Walters Direct Testimony, p. 33, ln. 477 – p. 34, ln. 516.

Q. Did Mr. Sagel warn the ICC that its failure to authorize a common equity ratio consistent with his recommendation may impair AIC's credit rating and increase its cost of debt?

A. Yes. Mr. Sagel specifically testified that "To the extent Ameren Illinois' credit ratings were downgraded, the Company's access to required debt capital to finance its operations could become more challenging and likely more expensive, which would be harmful to the Company's customers."[22]

Q. Was AIC's credit rating downgraded due to the ICC authorizing a lower common equity ratio?

A. No.

Q. Did AIC's cost of debt increase after the ICC issued its order authorizing a lower common equity ratio and a lower authorized ROE?

A. No, as is evident from my previous chart showing the yields on AIC's and Ameren Missouri's debt for the period June 30, 2023, through February 6, 2025.

PRO FORMA IMPACT OF CAPITAL STRUCTURE ON CREDIT PROFILE

Q. Did Mr. Sagel quantify the potential impact the Commission's adoption of your capital structure recommendation may have on Ameren Missouri's FFO/debt ratios?

A. Yes. Mr. Sagel estimates that if Ameren Missouri's revenue requirement in 2024 had been premised on my recommended capital structure containing a 42% common equity ratio, it would cause Moody's FFO/debt ratio to be approximately ** _____ **.[23] This estimate compares to the ** _____ ** actual FFO/debt achieved by Ameren Missouri in 2024.[24]

Q. Do you agree with his *pro forma* estimates?

A. No.

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[22] ICC Docket Nos. 22-0487 and 23-0082, Darryl T. Sagel Rebuttal Testimony, p. 15, lns. 307-309.
[23] Sagel Rebuttal, p. 26, lns. 9-11.
[24] *Id.*, p. 24, lns. 20-22.

Q. What about his methodology?

A. His methodology is reasonable.

Q. Why do you disagree with his estimates?

A. Mr. Sagel calculated his *pro forma* adjustments based on Ameren Missouri's estimated total capital and rate base as of December 31, 2024, which would impact subsequent cash flows. Because Ameren Missouri's 2024 FFO/debt ratios are premised on rates in effect for 2024, the *pro forma* adjustments should be calculated based on parameters used to determine the rates in effect in 2024. These parameters were determined in Ameren Missouri's 2022 rate case, Case No. ER-2022-0337 and Ameren Missouri's 2021 natural gas distribution rate case, Case No. GR-2021-0241. Ameren Missouri's total long-term capital was about $2.961 billion less as of the true-up date, December 31, 2022, as compared to December 31, 2024. Ameren Missouri's electric utility rate base was approximately $2.759 billion lower.

Because the parties did not specify an underlying capital structure or ROR in their black box stipulation and agreement in the 2022 electric utility rate case, the capital structure supporting 2024 rates is ambiguous. Staff and Ameren Missouri recommended a 51.91% common equity ratio and OPC recommended a 43% common equity ratio. For sake of estimating the potential largest *pro forma* impact on Ameren Missouri's 2024 FFO, I estimated the *pro forma* impact on Ameren Missouri's 2024 FFO by applying the full difference of Ameren Missouri's recommended 51.91% equity ratio to a 42% equity ratio. I estimate that Ameren Missouri's FFO/debt ratios would have been **_____ ** compared to the actual of **_____ **, or a difference of **____ **.

Q. What FFO/debt ratios does Moody's expect for Ameren Missouri on a going forward basis?

A. Approximately 19% to 21%.[25]

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[25] *Id., p. 2.*

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Q. If the Commission sets Ameren Missouri's ROR based on your recommended capital structure, what impact would the approximate ** _____ ** reduction to Ameren Missouri's FFO/debt ratio have on Ameren Missouri's projected FFO/debt ratios?

A. It would be approximately ** ______________ **, which is below the 17% threshold Ameren Corp bargained for itself from Moody's.

Q. Would this reduction cause Ameren Corp's FFO/debt ratios to be lower than Ameren Missouri's FFO/debt ratios?

A. Only if Ameren Corp maintains the current proportion of holding company debt in its consolidated capital structure.

Q. If the Commission adopted your recommended capital structure, could Ameren Missouri's Moody's credit rating be downgraded by a notch?

A. Probably not. The rate base for Ameren Missouri's natural gas utility operations is only approximately 3% of Ameren Missouri's combined electric and natural gas utility rate base. However, under the hypothetical scenario that my capital structure was applied to all of Ameren Missouri's rate base, then yes.

Q. Are you aware of any other Missouri utility companies that have an FFO/debt ratio below that of the hypothetical scenario for Ameren Missouri's natural gas utility operations?

A. Yes. Moody's assigns Evergy Missouri West a 'Baa3' rating despite Moody's expectation that EMW will have an FFO/debt ratio of 12% to 13% over the next 2-3 years.[26] Ameren Missouri's FFO/debt ratios would be in between this range and its current projected range of 19% to 21%.

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[26] Jillian Cardona and Michael Haggarty, "Rating Action: Moody's Ratings downgrades Evergy Missouri West to Baa3; outlook stable," Moody's Ratings, April 29, 2025.

Q. If the Commission were to adopt your recommended capital structure in this case, what could be done to improve Ameren Missouri's credit profile?

A. Ameren Corp could issue more common equity and less holding company debt to reduce the amount of financial risk in its consolidated capital structure. If Ameren Corp adjusted its capital structure to include a higher proportion of common equity, I would likely recommend this higher common equity ratio in Ameren Missouri's next rate case, which would improve its credit metrics.

PARENT/SUBSIDIARY FINANCING RELATIONSHIP

Q. Does an increasing amount and percentage of holding company debt cause financial instability for the entire Ameren Corp enterprise?

A. Yes. S&P Global Ratings clearly states that Ameren Missouri does not have sufficient insulation mechanisms in place to allow it to have a separate and distinct credit rating from Ameren Corp. Therefore, Ameren Corp's financial and business risks impact the rating S&P Global Ratings assigns to Ameren Missouri.

Q. Have other jurisdictions denied proposed acquisitions due, in part, to the financial instability that would be caused by issuing too much holding company debt to fund the acquisition?

A. Yes. This concern was one of the factors the Kansas Corporation Commission's ("KCC") cited in its disapproval of Great Plains Energy's proposed acquisition of Westar Energy.

Q. Did Great Plains Energy and Westar Energy eventually merge?

A. Yes, but only after they restructured the transaction to be a merger of equals ("MOE"), which is essentially a transaction in which each company's shareholders swap their shares for a pro-rated ownership interest in the combined company. Unlike the initial proposed transaction, this type of transaction did not involve use of leverage at the holding company.

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Q. Did the KCC impose any conditions on the merger to control the potential of Evergy issuing a disproportionate share of holding company debt to leverage its returns after the merger closed?

A. Yes. A condition of the KCC's approval of the merger was to institute an Earnings Review and Sharing Plan ("ERSP"). The KCC understood that the newly formed entity, Evergy, could attempt to retain more earnings for its shareholders by using more debt leverage at the holding company level as compared to its subsidiaries. Consequently, to the extent Evergy's consolidated common equity ratio was lower than its subsidiaries' common equity ratios by 2.5% to 3.5%, the percentage of equity allowed to be counted for the ERSP would be reduced by a proportionate amount.

Q. How much lower is Ameren Corp's equity ratio than Ameren Missouri's common equity ratio?

A. As of September 30, 2024, the difference between Ameren Cop's common equity ratio and Ameren Missouri's common equity ratio reached an all-time high of 11.76 percentage points. Ameren Corp has steadily increased the amount and proportion of holding company debt as compared to Ameren Missouri since the passage of PISA, when it began investing significant amounts of capital in Missouri.

Q. What common equity ratio did the KCC authorize Evergy's subsidiaries to utilize for purposes of the ERSP?

A. 51% in 2019, 50.5% in 2020 and 50% in 2021 through 2022.

Q. What was Evergy's common equity ratio over this period?

A. It was in the 47% to 49% range.

Q. When did the ERSP expire?

A. At the time Evergy's Kansas' new rates took effect, which was at the end of 2023.[27]

[27] Docket Number D-23-EKCE-775-RTS

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Q. What have Evergy's common equity ratios been since the ERSP expired?

A. Evergy's common equity ratios have been in the range of 44% to 46%.

Q. What is Ameren Corp's consolidated common equity ratio?

A. Around 40% to 41% without short-term debt, and around 39% to 40% with short-term debt. Ameren Corp's common equity ratio has gradually declined from approximately 48% in 2018 to its current level, as documented in my rebuttal testimony.

Q. Had investors historically believed that the Commission's potential consideration of Ameren Corp's use of holding company debt in setting Ameren Missouri's ROR restrained Ameren Corp from being overly aggressive in its use of holding company debt?

A. Yes. Wells Fargo stated the following in a report published on Ameren Corp in 2023:

> AEE's '23-27 new equity needs total $2.8B, consisting of $2.3B of external equity and $100M annually under DRPlus [dividend reinvestment plan] and internal programs. AEE continues to target a parent equity ratio of ~45%. The equity guidance is consistent with our assumption and '23 needs of $0.4B represent ~1.5% of market cap. **AEE employs a relatively conservative financing strategy vs. peers, likely reflecting regulatory-related look-through considerations in MO.** (emphasis added)[28]

Q. Mr. Sagel testifies that the common equity Ameren Corp invested in Ameren Missouri's capital structure was raised through Ameren Corp's external equity issuances.[29] Therefore, because this is the capital that supports Ameren Missouri's rate base, Ameren Missouri's capital structure should be used for the authorized ROR.[30] First, do you agree that tracing the capital to external issuances should be the determining factor for assessing a fair and reasonable capital structure?

A. No. Ameren Corp's equity issuances benefit the entire enterprise's credit profile, not just Ameren Missouri's credit profile. A recognized principle of finance is that the risk of the investment determines the cost of capital, not the source of funds. Based on Mr. Sagel's

[28] Neil Kalton, et. al., "AEE: Quick Take on Q4 Updates – All Looks Just Fine," Wells Fargo, February 15, 2023.
[29] Sagel Rebuttal, p. 8, ln. 3 – p. 10, ln. 10.
[30] Id.

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logic, if Ameren Corp only sourced third-party equity for equity infusions into Ameren Missouri, but issued holding company debt to infuse equity into its other subsidiaries, only Ameren Missouri's capital structure would be legitimate. It is this logic that supports S&P's family ratings approach to assigning credit ratings based on the parent company's consolidated credit profile.

Q. Second, do you agree with Mr. Sagel's assertion that Ameren Corp's equity contributions into Ameren Missouri are traceable to Ameren Corp's external common equity issuances?

A. No. I addressed this issue in my rebuttal testimony when responding to Dr. Won's direct testimony. Mr. Sagel testifies that Ameren Corp's $350 million common equity contribution to Ameren Missouri during the second quarter of 2024 was funded by Ameren Corp's issuance of external common equity in 2023. Mr. Sagel's testimony can only be accurate if for some reason Ameren Corp issued common equity in 2023 and deposited the funds in a cash account for later investment in Ameren Missouri. Of course, doing so is neither efficient nor practical. Ameren Corp's cash balance as of December 31, 2023, was $25 million, which was much lower than the $318 million in proceeds from Ameren Corp's issuance of common equity during the fourth quarter of 2023.

Q. How did Ameren Corp use the $318 million of funds it raised from its issuance of common equity during the fourth quarter of 2023?

A. It is difficult to pinpoint exactly how Ameren Corp used the $318 million of common equity proceeds because it also issued $1.3 billion in holding company debt during the same quarter. However, because Ameren Corp did not make equity contributions to Ameren Missouri during the same quarter, investment in Ameren Missouri can be ruled out. As of September 30, 2023, Ameren Corp had $1.124 billion in short-term debt outstanding. Additionally, Ameren Corp paid $166 million in dividends during the fourth quarter of 2023. Therefore, it appears the funds from Ameren Corp's holding company securities issuances were primarily used to refinance short-term debt and fund Ameren Corp's dividend to third-party shareholders.

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Q. Mr. Sagel asserts that your direct testimony suggests Ameren Missouri's dividend payout ratio should be similar to Ameren Corp's.[31] Is he correct?

A. No. I asserted in my testimony that if Ameren Missouri were managed as if it were a stand-alone entity, it would have a carefully managed dividend payment policy, similar to Ameren Corp's targeted dividend payout ratio in the range of 55% to 65%.

Q. What did you intend to convey?

A. That if Ameren Missouri were a stand-alone entity, as it was prior to the formation of Ameren Corp in 1997 as the holding/parent company of Ameren Missouri and its affiliates, it would be expected to fund a consistent quarterly dividend to third-party shareholders. As a stand-alone entity, accountable to third-party shareholders, it would be obligated to fund the dividend regardless of its cash flow position (*i.e.* free cash flow negative due to increased investment needs or free cash flow positive due to reduced investment needs).

Q. Mr. Sagel testifies that the fact that Ameren Corp "had to lean more on parent company debt" to fund dividends during Ameren Missouri's current, capital-intensive spending cycle proves Ameren Missouri's financial independence as it relates to managing its capital structure in a responsible and prudent manner as its cash flow position has changed.[32] Do you agree?

A. No. First, I take issue with Mr. Sagel's characterization that Ameren Corp had to "lean more on parent company debt" to fund dividends. Ameren Corp did not *have* to "lean more on parent company debt" to fund dividends, it *chose* to. Ameren Corp's ability to issue debt is a function of its ownership of its regulated utility subsidiaries. Ameren Corp has no assets other than its regulated utility subsidiaries. Its balance sheet capacity is dependent on these low-risk regulated utilities, not independent of them. Ameren Corp's shared credit facilities with Ameren Missouri and AIC allow it access to commercial paper markets. The decision of Ameren Corp's officers and BOD to issue commercial paper at the holding

[31] Sagel Rebuttal, p. 11, l. 7 – p. 12, l. 21.
[32] Sagel Rebuttal, p. 12, lines 11-21.

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company rather than at Ameren Missouri to fund third-party dividends is a matter of choice, not need.

Second, if Ameren Corp were a third-party shareholder of Ameren Missouri, similar to shareholders of Union Electric prior to 1997, it would expect a consistent quarterly dividend from Ameren Missouri despite Ameren Missouri's cash flow position. For example, Union Electric was expending significant amounts of capital in the late 1970s and early 1980s during the building of its Callaway Nuclear Plant. Nevertheless, it not only maintained the dividends paid to third-party shareholders, but its dividends increased at a compound annual growth rate ("CAGR") of approximately 3.2%. Because Union Electric was truly an independent entity responsible to third-party shareholders, it issued its own short-term debt to finance its construction needs while still maintaining investors' expected dividends.

Q. Dr. Won testifies that Ameren Missouri "has neither internally identified nor externally communicated a targeted capital structure." What is Dr. Won's basis for his testimony?

A. Ameren Missouri's response to Staff Data Request No. 0117 (Schedule DM-S-3 attached).

Q. Is Ameren Missouri's response to Staff's data request consistent with its actions and testimony?

A. No. Ameren Missouri's requested common equity ratio for its general rate cases since at least 2012 has been in the range of 51.75% to 52.30%.[33] Although Ameren Missouri's almost constant approximate 52% common equity ratio speaks for itself, Mr. Sagel's direct testimony confirms its deliberate targeting of an approximate 52% common equity ratio since at least 2016.[34]

[33] Murray Direct, p. 41, lns. 3-6.
[34] Sagel Direct, p. 12, ln. 18 – p. 13, ln. 4.

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Q. Do the capital flows between Ameren Corp and Ameren Missouri establish that Ameren Missouri's capital structure is not the result of arms-length transactions?

A. Yes. I agree with Mr. Sagel that the "use of funds invested gives rise to the risk of the investment."[35] The purest insight as to Ameren Corp's view about the business risk associated with investing in its regulated utility subsidiaries is the capital structure it maintains at the consolidated level. It is this capital structure that has the competing interests of achieving the lowest reasonable cost of capital, while maintaining an equity layer that ensures financial stability of the entire enterprise. If Ameren Corp wants its utilities' ratepayers to pay for a higher-cost, equity-rich capital structure, it should issue more common equity at the holding company level, which would provide ratepayers the benefit of a financially stronger parent company. Instead, Ameren Corp's higher leverage is a credit constraint on Ameren Missouri.

Q. Does the basic financial principle—that the required return is related to the use of the funds and not the source of the funds—also contradict Mr. Sagel's opinion that Ameren Missouri's capital structure is legitimate if Ameren Corp's equity contributions to Ameren Missouri are sourced from Ameren Corp's issuance of common equity?

A. Yes. Mr. Sagel's attempt to claim that Ameren Missouri's per books capital structure is legitimate if the source of Ameren Missouri's equity infusion was third-party common equity issued by Ameren Corp, contradicts his own position that it is the use of the funds and not the source of the funds that influences the cost of capital. I agree that the risk of the underlying investment drives the cost of capital and determines the amount of debt leverage that can reasonably be used. Ameren Corp's more leveraged capital structure captures managements' sincere view of its low-risk regulated utility assets' debt capacity.

[35] Sagel Rebuttal, p. 8, ll. 12-14.

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Q. Has Mr. Sagel testified in the past that Ameren Missouri needs more common equity than AIC because it is an integrated-electric utility while AIC is a distribution-only utility?

A. Yes. As recently as Ameren Missouri's 2019 rate case, Mr. Sagel testified as follows in his rebuttal testimony:

> Given the higher-risk nature of Ameren Missouri's vertically-integrated business, (with numerous energy centers including one nuclear center) relative to the risk of Ameren Corporation's other primary subsidiaries (Ameren Illinois operates electric transmission and distribution facilities and natural gas delivery facilities), it stands to reason that Ameren Missouri would support and maintain a common equity ratio that is higher than Ameren Corporation's consolidated equity ratio.[36]

and

> The lower overall risk profile of Ameren Illinois relative to Ameren Missouri is also evident in Ameren Illinois' stronger issuer rating at Moody's, which rates Ameren Illinois A3 and Ameren Missouri Baa1. Moody's ratings for each of Ameren Illinois and Ameren Missouri are independently developed based on their discrete credit profiles.[37]

Q. What are AIC's and Ameren Missouri's current Moody's credit ratings?

A. Moody's still rates AIC one notch higher at 'A3' as compared to Ameren Missouri's 'Baa1' rating.[38]

Q. What was AIC's ratemaking common equity ratio at the time Mr. Sagel argued AIC's capital structure should be managed to a lower common equity ratio due to the lower risk profile of its operations?

A. 50%.

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[36] Case No. ER-2019-0335, Darryl T. Sagel Rebuttal, p. 14, lines 3-8.
[37] *Id.,* p. 31, lines 5-8.
[38] Moody's Ratings Credit Opinion on Union Electric Company, May 13, 2024.

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Q. What common equity ratio did Mr. Sagel suggest should be used for purposes of setting AIC's rate of return in its recent multi-year rate plan application before the ICC?

A. Mr. Sagel sponsored capital structure testimony on January 20, 2023, before the ICC where he requested that AIC's electric utility rates be set based on an approximate 54% common equity ratio over the four-year period of the multi-year rate plan.[39]

Q. What common equity ratio did the ICC authorize AIC for purposes of the multi-year rate plan for its electric utility operations?

A. 50%.

Q. What is ATXI's per books common equity ratio?

A. Approximately 60%.

Q. Is ATXI's common equity ratio consistent with Mr. Sagel's testimony that Ameren Missouri's affiliates can incur a higher percentage of debt because of lower business risk?

A. No. Despite the fact Ameren Corp's ATXI subsidiary has the lowest business risk of its three primary operating subsidiaries, its balance sheet implies that it requires the highest common equity ratio. The fact that this implication is clearly not true provides further evidence that Mr. Sagel's testimony is not credible.

Q. Can you provide corroborating evidence which demonstrates that ATXI is considered Ameren Corp's lowest-risk subsidiary?

A. Yes. Both Moody's and S&P consider transmission-only companies subject to FERC rate regulation to have the least amount of business risk of most utility subsectors, with the only exception being water utility companies. S&P assesses the financial risk of transmission-only companies, such as ATXI, against low-volatility benchmarks, as compared to medial volatility benchmarks for vertically-integrated electric utility companies. In Moody's most

[39] Ameren Illinois Company Petition for Approval of a Multi-Year Rate Plan pursuant to 20 ILCS 5/16-108.18, Docket No. 23-0082, Darryl T. Sagel Direct, January 20, 2023 - Document for 23-0082 (illinois.gov)

recent report assessing the risk profiles of Ameren Corp's subsidiaries, it ranked ATXI, AIC and Ameren Missouri as follows (from least business risk to most business risk): (1) ATXI, (2) AIC, and (3) Ameren Missouri.[40]

Additionally, Wall Street equity analysts typically assign the highest price-to-earnings ("P/E") multiples to FERC-regulated transmission earnings because of the low-risk nature of these assets.

Q. Considering the general rank-order of Ameren Corp's subsidiaries' business-risk profiles, why are the targeted common equity ratios the opposite of Mr. Sagel's explanation of basic risk and return principles?

A. Because the subsidiaries' capital structures are primarily managed for ratemaking purposes, not achieving the lowest reasonable cost of capital consistent with the underlying business risk. Ameren Corp achieves the lowest reasonable cost of capital at the consolidated level.

Q. How can this Commission ensure Ameren Missouri's ratepayers are charged for a market-driven capital structure rather than a ratemaking-driven capital structure?

A. Consider Ameren Corp's consolidated capital structure strategies. This capital structure is the only one with the competing interest of being managed to achieve a lower cost of capital for the benefit of its shareholders, while also minimizing the issuance of additional third-party common equity to reduce dilution of earnings to existing shareholders. If Ameren Corp desires to be awarded a ROR consistent with Ameren Missouri's higher-cost capital structure, then it should issue additional common equity to third-party equity investors.

[40] Moody's Credit Opinion on Ameren Corporation, May 15, 2024.

INVESTOR EXPECTATIONS ON RATEMAKING CAPITAL STRUCTURE

Q. Mr. Sagel discusses market responses to the Commission's deliberations in the Spire Missouri gas rate cases, Case Nos. GR-2017-0215 and GR-2017-0216, to justify why the Commission should accept Ameren Missouri's proposed capital structure.[41] Do you think market responses like these should be the Commission's primary focus when setting rates?

A. No. Even as a consumer advocate witness, I consider the potential impact on a company's investors when making my recommendations; but a negative stock price reaction is not proof of a "bad" Commission decision. Investors' expectations are impacted by many different factors, with anticipated Commission decisions being one of the primary factors. Investors price in the probability of expected outcomes in rate cases. If a particular commission has consistently awarded higher ROEs with equity-rich capital structures, investors price in these investor-friendly outcomes in their projections. Additionally, companies' guidance regarding discrete earnings per share ("EPS") expectations as well as company guidance on long-term CAGR in EPS greatly influences investors' expectations. Ameren Corp has consistently guided investors to an expected 6% to 8% long-term CAGR in EPS. However, this earnings guidance has many assumptions underlying it.

Earnings guidance, for a pure-play regulated utility such as Ameren Corp, has a few key factors typically influencing it. The first factor is anticipated rate base growth. The second factor is the probability of recovery of this increased investment. The third factor regards the parameters applied to the rate base for purposes of allowed returns (which include an assumed capital structure and potential allowed ROEs).

Consider a situation where the basis of Ameren Corp's guidance to investors on earnings expectations is that Ameren Missouri's authorized ROR will be based on a 52% ratemaking common equity ratio. The Commission then authorizes a lower common equity ratio with the same projected authorized ROE. The result would be that Ameren Corp's stock price will adjust for revised expectations. Again, a stock price decline due to a more reasonable

[41] Sagel Rebuttal, p. 43, l. 6 – p. 44, l. 11.

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authorized capital structure is simply a reset of investors' expectations rather than an indication of a punitive decision.

As I explained in Spire Missouri's 2022 rate case, Case No. GR-2022-0179, because Spire Inc. guided investors to expect Spire Missouri's rates to be set at a 54% common equity ratio, it was no surprise that Spire Inc.'s stock price declined when the Commission ordered a lower ROR based on a capital structure with a lower common equity ratio. A stock price decline is not proof of an unfair outcome to investors, but rather an outcome that is different from investors' expectations.

FOUR CRITERIA – SUBSIDIARY VS. PARENT CAPITAL STRUCTURE

Q. Do Dr. Won and Mr. Sagel cite similar criteria to support their view that Ameren Missouri's per books capital structure is appropriate for setting Ameren Missouri's ROR in this case?

A. Yes. Both Dr. Won and Mr. Sagel believe the following criteria support their argument to use Ameren Missouri's per books capital structure to set its authorized ROR:

1. Whether the subsidiary utility obtains all of its capital from its parent, or issues its own debt and preferred stock;
2. Whether the parent guarantees any of the securities issued by the subsidiary;
3. Whether the subsidiary's capital structure is independent of its parent (i.e. existence of double leverage, absence of proper relationship between risk and leverage of utility and non-utility subsidiaries);
4. Whether the parent (or consolidated enterprise) is diversified into non-utility operations.[42]

Mr. Sagel and Dr. Won appear to agree on why they believe the first three criteria support the use of Ameren Missouri's per books capital structure to set its authorized ROR. However, while both witnesses believe the fourth criterion supports the use of Ameren Missouri's capital structure, they have opposite rationales for that belief.

[42] David Parcell, "The Cost of Capital – A Practitioner's Guide," 2010 Edition, p. 46.

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Q. Did you address any aspects of these criteria in your rebuttal testimony?

A. Yes. While Dr. Won did not specifically cite the above-criteria in his direct testimony, he testified about several factors similar to these criteria that he believes supports using Ameren Missouri's capital structure.[43] The factors Dr. Won discussed in his direct testimony closely follow Mr. Sagel's response to Dr. Won's Data Request No. 0130 attached as Schedule DM-S-4.

Q. How do Mr. Sagel's responses to Dr. Won's data request address the four criteria?

A. As it relates to the first factor, Dr. Won requested that Ameren Missouri either affirm or deny whether it has executed affiliate notes (short-term or long-term) with Ameren Corp (item numbers 1 and 2 in Dr. Won's data request). Other than money pool borrowings, Mr. Sagel denies that Ameren Missouri has executed affiliate notes with Ameren Corp. Therefore, based on Mr. Sagel's response and the fact that Ameren Missouri issues its own long-term and short-term debt, Dr. Won and Mr. Sagel agree that the first factor supports use of Ameren Missouri's capital structure.

Although it is a fact that Ameren Missouri issues its own short-term debt and long-term debt, the fact that Ameren Corp shares a credit facility with Ameren Missouri should also be considered. Ameren Missouri's credit quality allows both Ameren Corp and Ameren Missouri to access short-term debt capital markets. It is Ameren Corp's choice to issue short-term debt at the holding company level to fund dividends rather than doing so at Ameren Missouri. Ameren Missouri was able to fund and grow its dividends to third-party investors before Ameren Corp became its holding company.

Item numbers 5 and 6 of Dr. Won's DR No. 0130 address the second criterion as to whether Ameren Corp guarantees any of Ameren Missouri's debt issuances. I agree with Mr. Sagel and Dr. Won that Ameren Corp does not guarantee Ameren Missouri's debt. However, Ameren Corp derives its creditworthiness from its regulated utilities, which includes Ameren Missouri. As proven by Ameren Corp's startup investment in ATXI, it used cash flows from its regulated utility subsidiaries to subsidize affiliate capital investment needs.

[43] Won Direct, p. 34, l. 10– p. 36, l. 15.

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Ameren Corp's ability to issue holding company debt is a function of its ownership of its regulated utilities, including Ameren Missouri. Ameren Corp does so at the expense of Ameren Missouri's credit quality and a higher ROR charged to ratepayers.

Dr. Won's Data Request No. 0133 to Ameren Missouri relates to the third criterion. As can be seen in Schedule DM-S-5, Dr. Won first provided his definition of "double leverage." He then asked if Ameren Corp employs double leverage in its financing strategies. Ameren Missouri denies that its parent company employs double leverage, at least based on Dr. Won's definition. I disagree with Ameren Missouri's response. Although it is true that it does not appear that Ameren Corp has directly used proceeds from long-term debt to contribute common equity capital to Ameren Missouri, double leverage should not be limited to these constraints. Double leverage is simply the issuance of debt at a holding company and at the operating subsidiaries. However, even with this in mind, Ameren Corp's financing source for its equity contribution to Ameren Missouri during the second quarter of 2024 was short-term debt. Ameren Corp's short-term debt balance of over $1 billion at September 30, 2023, was refinanced with Ameren Corp long-term debt and common equity in the fourth quarter of 2023. It is difficult to reconcile the specific purposes for which Ameren Corp issued short-term debt, but as Mr. Sagel testifies, Ameren Corp often issues holding company financing to fund dividends it has chosen not to receive from its subsidiaries.[44] Therefore, Ameren Corp's regular and more significant holding company financing activities are trending to more financial integration rather than less.

Q. What is Ameren Corp's motivation for employing double leverage?

A. Ameren Corp can achieve a lower cost of capital for investments in its utilities without sharing this lower cost with its subsidiaries' ratepayers. In Ameren Corp's case, it only owns regulated utility assets and it has a much more leveraged consolidated capital structure than its subsidiaries, which proves that there is an absence of a proper relationship

[44] Sagel Rebuttal, p. 12, lns. 11-13.

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between risk and return. But for Ameren Corp's ownership of low-risk regulated utilities, it would not be able to raise holding company debt.

Q. Is the comparison of Ameren Missouri's business risk to that of its holding company, Ameren Corp, the premise of the fourth criterion listed above?

A. Yes. The fourth criterion, above, provides insight as to whether it is logical to expect the parent company's consolidated capital structure to be significantly different than that of its subsidiary, due to the parent's consolidated business risk being different than the business risk of the subsidiary. The criterion specifically identifies non-utility operations as a consideration because non-utility operations typically have higher business risk than monopoly utility operations. If a parent company's non-regulated and/or non-utility operations are insignificant, then it is not logical for the parent company to have a significantly different capital structure than its subsidiaries.

Q. Did Dr. Won request Ameren Missouri provide him information as it relates to the last criterion?

A. Yes. Item No. 8 of Dr. Won's Data Request, No. 0130, requested Ameren Missouri to identify the percentage of Ameren Corp's total assets that are considered non-utility assets. In response to Dr. Won's data request, Mr. Sagel indicated that 1.03% of Ameren Corp's total assets are considered "non-utility" assets.

Q. Did Dr. Won consider this information supportive of using Ameren Missouri's per books capital structure rather than considering Ameren Corp's consolidated capital structure?

A. Yes. Dr. Won considers this information supportive of adopting Ameren Missouri's capital structure. He testifies as follows in his direct testimony:

> In addition, Ameren Corp.'s non-utility assets are around 1.3% [sic] of its total assets. Hence, there are no significant concerns about the financial relationship between Ameren Missouri's regulated utility service and Ameren Corp's non-regulated business.[45]

[45] Won Direct, p. 36, lines 4-6.

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Q. Is the fact that Ameren Corp is essentially a pure-play regulated utility supportive of accepting Ameren Missouri's per books capital structure as fair and reasonable for setting Ameren Missouri's ROR?

A. No. Dr. Won testifies that he is not concerned about the financial relationship between Ameren Missouri's regulated utility service and Ameren Corp' non-regulated business. I am not concerned about this interrelationship either. In fact, if Ameren Corp had more non-regulated operations, then it would be reasonable to expect Ameren Corp to have a higher common equity ratio than Ameren Missouri.

For example, Algonquin Power & Utilities Corp ("APUC"), the ultimate parent holding company of The Empire District Electric Company, had historically been comprised of approximately 20-25% of non-regulated utility operations through its wholly-owned subsidiary, Algonquin Power Company. APUC had targeted a higher common equity ratio for its non-regulated subsidiary, Algonquin Power Company, versus a lower common equity ratio for its regulated utility subsidiary, Liberty Utilities Company.[46] The higher common equity ratio at Algonquin Power Company was not consistent with the lower-risk profile of Liberty Utility Company's regulated utilities, but this higher common equity is consolidated at APUC. Using APUC's consolidated capital structure in such a situation would have resulted in ratepayers paying for a higher common equity ratio than that which is consistent with the risk level of APUC's regulated utility subsidiary.

Q. Did Dr. Won ask you to provide further clarification about your testimony which discusses the increasing difference between the proportion of leverage in Ameren Corp's consolidated capital structure compared to Ameren Missouri's capital structure?

A. Yes. Please see the attached Schedule DM-S-6 which is my response to Dr. Won's data request. Although my testimony provides much of my rationale for recommending consideration of Ameren Corp's capital structure for purposes of authorizing a fair and reasonable ratemaking capital structure for Ameren Missouri, I would like to expand a little further on my response to Dr. Won's data request. While I am not aware of any specific

[46] Case No. ER-2021-0312, Todd Mooney Rebuttal, p. 13, l. 17 – p. 14, l. 7.

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journal articles addressing disparities in parent companies' capital structures and their subsidiary capital structures in terms of utility ratemaking, estimating the cost of capital is not unique to the utility industry.

As I explained in my response to Dr. Won's data request, while I am not aware of any specific journal articles addressing the specific utility ratemaking debate about considering the disparity between a parent company's use of leverage and its subsidiaries' use of leverage, estimating the cost of capital for divisions and projects is common in corporate finance. If a division or project is considered to be similar in risk profile to the parent company's overall risk profile, then the principles of capital budgeting recommend the use of the firm's cost of capital. The following is an excerpt from an authoritative corporate finance textbook:

> **DIVISIONAL AND PROJECT COSTS OF CAPITAL**
>
> As we have seen, using the WACC as the discount rate for the future cash flows is only appropriate when the proposed investment is similar to the firm's existing activities. This is not as restrictive as it sounds. If we were in the pizza business, for example, and were thinking of opening a new location, then the WACC is the discount rate to use. The same is true of a retailer thinking of a new store, a manufacturer thinking of expanding production, or a consumer products company thinking of expanding its markets.[47]

The same is true for a subsidiary of a pure-play regulated utility such as Ameren Corp which only owns regulated utility companies. Ameren Corp's cost of capital is the appropriate WACC to apply to projected cash flows from investments in Ameren Missouri's utility systems. Ameren Corp's WACC is a function of not only the low business risk of its regulated utility subsidiaries, but also its ability to more liberally use debt capital to fund its utilities' capital expenditures.

[47] Ross, Westerfield and Jordan, "Fundamentals of Corporate Finance," Richard D. Irwin Inc, 1992, p. 500.

OTHER DR. WON CAPITAL STRUCTURE ISSUES

Q. What ratemaking capital structure did Dr. Won recommend be used to set Evergy Missouri West's authorized ROR in Case No. ER-2024-0189?

A. Dr. Won recommended a ratemaking capital structure consisting of 50% common equity and 50% long-term debt.

Q. What was the basis for Dr. Won's recommended capital structure in that case?

A. Dr. Won testified that his recommended ratemaking capital structure was consistent with Evergy's targeted capital structure for Evergy and EMW of just over 50% common equity.[48]

Q. What did EMW represent as its actual common equity ratio when it filed its direct testimony?

A. As of June 30, 2023, EMW witness Kirkland B. Andrews represented that EMW's capital structure consisted of 53.52% common equity.

Q. What common equity ratio did EMW target for purposes of the true-up date of June 30, 2024?

A. 52.04%.

Q. According to EMW, what was its actual common equity ratio at June 30, 2024?

A. Approximately 50%. EMW decided to issue $300 million of long-term debt rather than the $200 million it had projected at the time it filed its direct testimony.

Q. Could Ameren Missouri also adjust its capital structure to a more reasonable 50% common equity ratio as of the true-up date in this case?

A. Yes. Instead of Ameren Missouri retaining all its net income, which is not customary for a stand-alone utility company, Ameren Missouri could distribute a dividend to Ameren

[48] Case No. ER-2024-0189, Won Direct, p. 29, lns. 17-19.

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Corp and issue its own short-term debt to initially finance its capital expenditures. These transactions would allow Ameren Missouri to achieve a 50% common equity ratio.

Q. After the ICC authorized a ratemaking common equity ratio of 50% for AIC in its rate cases during the period of its formula rates, did Ameren Corp manage AIC's capital structure to target this common equity ratio?

A. Yes. Ameren Corp targeted a 50% common equity ratio starting in 2016 and maintained AIC's common equity ratio at this level until 2020.[49]

Q. Did EMW provide anything more specific when it indicated it was targeting a common equity ratio of "just over 50% equity?"

A. No. In my opinion, just over 50% could be anywhere between 50% to 52.5%. Based on EMW's initial projection of an approximate 52% common equity ratio at the true-up date, it considered this ratio to be "just over 50%".

Q. Did Evergy recently file a new rate case for its Kansas utility subsidiaries, Evergy Kansas Central, Inc. ("EKC") and Evergy Kansas South, Inc. ("EKS")?

A. Yes.

Q. What common equity ratio did Evergy request in those rate cases?

A. 51.97%, which is its projected common equity ratio as of March 31, 2025.[50]

Q. What do Ameren and Evergy have in common?

A. They both have holding companies that actively issue holding company debt (both short-term and long-term debt). This dynamic allows them to manage their inter-affiliate capital flows to ensure an actual operating capital structure consistent with their requested common equity ratio of 52%.

[49] ICC Docket No. 22-0487 and 23-0082, Darryl T. Sagel Rebuttal Testimony, p. 3, lns. 53-56.
[50] Kansas Corporation Commission, Docket No. 25-EKCE-294-RTS, Direct Testimony of Geoffrey T. Ley, p. 18, Table 1.

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Q. What appears to be the only difference in Dr. Won's decision to recommend a 50% common equity ratio for EMW and a 52% common equity ratio for Ameren Missouri?

A. Differing responses to Dr. Won's data requests. In the EMW rate case, EMW's response to Dr. Won's DR indicated that it targets a capital structure of "just over 50%," whereas Ameren Missouri responded that it and Ameren Corp "has neither internally identified nor externally communicated a targeted capital structure." Therefore, if EMW provided a DR response similar to Ameren Missouri and Dr. Won followed the same logic, then he would have accepted EMW's actual capital structure.

Q. Was Ameren Missouri's response to Dr. Won's data request accurate?

A. No. As shown on page 51 of Ameren Corp's April 2024 Rating Agency presentation, Ameren Corp plans to target a consolidated common equity ratio of around **____ ** over the next three years and a **____ ** common equity ratio for Ameren Missouri through 2028. The fact that Ameren Corp plans to keep its subsidiaries' common equity ratios constant regardless of changes in regulatory, economic and business conditions demonstrates Ameren Missouri's response to Staff's DR is not credible. Ameren Corp claims to manage Ameren Missouri's capital structure to "specifically and continually maintain the balance of debt and equity in its capital structure to minimize its overall cost of capital and, at the same time, maintain financial strength and flexibility."[51] If that claim were true, it would be reasonable to expect some fluctuation based on changing business and regulatory conditions. As I have established, Ameren Corp's strategy is to minimize the cost of capital at the consolidated holding company level rather than at the subsidiary level, because this structure maximizes subsidiary cash flows through a higher revenue requirement but minimizes the cost of capital at a level that Ameren Corp hopes the Commission will ignore.

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[51] Citation

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Q. Even if a company does not explicitly communicate a targeted capital structure, is it reasonable to analyze its past capital structures to determine its target?

A. Yes. It is abundantly clear that Ameren Corp targets a constant 52% common equity ratio for Ameren Missouri as this has been its approximate common equity ratio for well over ten years and is expected to be its common equity ratio over the next five years.

Q. If the Commission authorized Ameren Missouri a common equity ratio of 50%, would there be a negative reaction from rating agencies?

A. Not if Ameren Missouri voluntarily requests a 50% common equity ratio. Although the impact on the credit metrics would be the same whether Ameren Missouri voluntarily requested it or the Commission imposed the lower common equity ratio, based on Evergy's past decisions to recommend a 50% common equity ratio, the rating agencies have not reacted negatively.

<u>CAPITAL STRUCTURE SUMMARY</u>

Q. Would you summarize your main points in response to Dr. Won's and Mr. Sagel's recommendations to use Ameren Missouri's capital structure to set Ameren Missouri's ROR?

A. Yes. Ameren Corp's actions speak louder than Ameren Missouri's words (testimony and data request responses). Holding companies can provide benefits to utility subsidiaries through certain economies of scale, but they can also be used to mislead as to the true market cost of capital related to its subsidiaries. If Ameren Corp had its own source of income, other than from its regulated utilities, it might be plausible to claim that Ameren Corp issues debt to assist its subsidiaries. That is not the case here.

Ameren Corp is a parent company that relies on the low-risk income of its subsidiaries to issue holding company debt rather than holding company equity to invest in equity in its subsidiaries. If Ameren Missouri issued this debt, rather than "leaning on" Ameren Corp, it would justly be captured in the ROR charged to Ameren Missouri's ratepayers. Ameren Corp exists because of Ameren Missouri, not vice versa. If Ameren Missouri was still

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directly accountable to third-party equity investors, its capital structure would be a function of market forces. Now it's a function of affiliate transactions to meet ratemaking targets.

ANN E. BULKLEY'S REBUTTAL TESTIMONY

RETURN ON EQUITY

Q. Ms. Bulkley testifies that there is no basis for your position that utility companies are authorized ROEs higher than their COE.[52] What is the basis for your opinion?

A. My own COE analysis. However, I also have consistently provided information from investor sources over the last fifteen years, which corroborate my position. Additionally, I have regularly discovered utility company internal valuation analyses that contradict the high COE estimates proffered in utility rate cases. Although the information I disclosed in other utility rate cases is confidential, I have regularly provided this information in Ameren Missouri rate cases since at least 2010.

Q. Are there any financial metrics that are often evaluated to determine if a company or portfolio of companies are earning more than their cost of capital?

A. Yes. Market-to-book ratios above one generally establishes that a company is creating value for its shareholders by earning more than its cost of capital.

Q. Why?

A. The simplest example to illustrate this dynamic is a bond valuation example. If a 30-year United States Treasury ("UST") bond is issued today at a coupon consistent with the current yield-to-maturity on 30-year UST bonds (4.1%), then the value of the bond is exactly equal to the $1,000 principal balance of the bond. If the market cost of debt increases to 4.5% in one year, investors would only pay $935.57 for the 4.1% coupon bond in order to ensure they receive the current market yield of 4.5%. The market-to-book ratio of the 4.1% bond is 93.56%. Conversely, if the market cost of debt decreased to 3.7% in one year, investors would pay $1,070.77 for the 4.1% coupon in order for the seller to be

[52] Bulkley Rebuttal, p. 69, ln. 14 – p. 70, ln. 14.

compensated for the lower coupons on newly-issued bonds. The market-to-book ratio of the 4.1% bond is 107.08% in this scenario. These same principles apply to the book value (original issue price) of common stock.

Q. How so?

A. Justified price-to-book ratios are determined through the following formula, which is premised on using discounted cash flow analysis:[53]

$$P_0/B_0 = (ROE - g)/(r - g)$$

Where:

P_0	=	price/market value at period 0
B_0	=	book value at period 0
ROE	=	expected return on common equity
g	=	growth in earnings
r	=	cost of common equity

If expected earnings are higher than the cost of common equity, then the justified market/book ratio is greater than one and vice versa.

Q. Can you provide the market-to-book ratios of the more pure-play utility companies within your proxy group?

A. Yes. See the following chart for the market-to-book ratios of Atmos, NiSource, Northwest, ONE Gas and Spire Inc.:

[53] Refresher Reading, 2024 CFA® Program, Level 2, p. 45.

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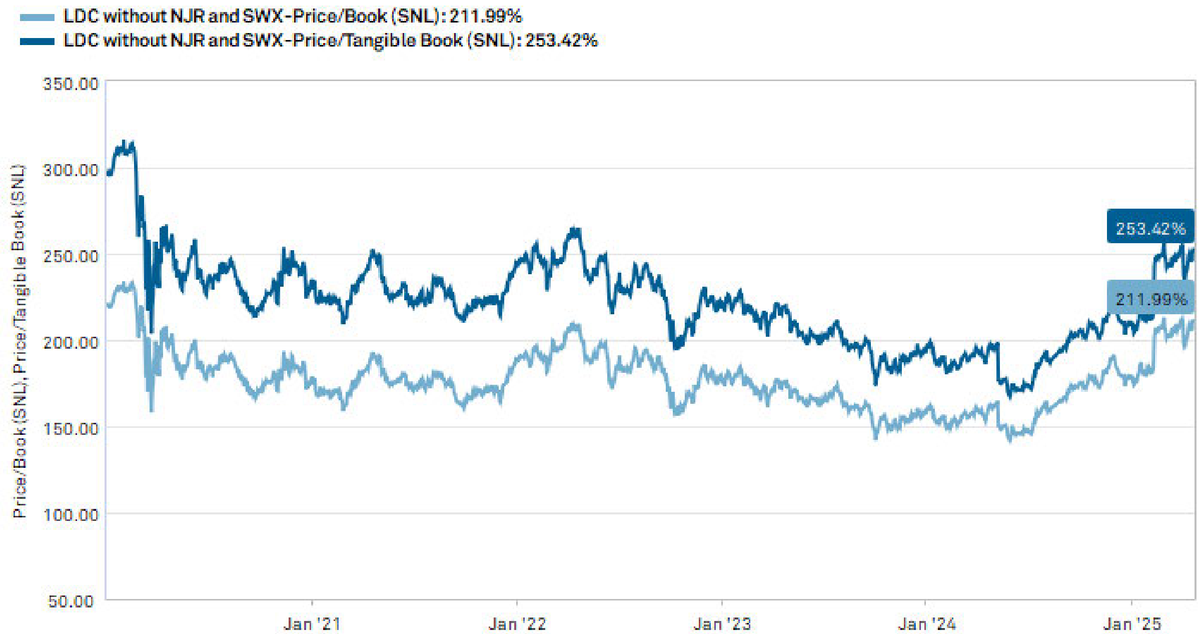
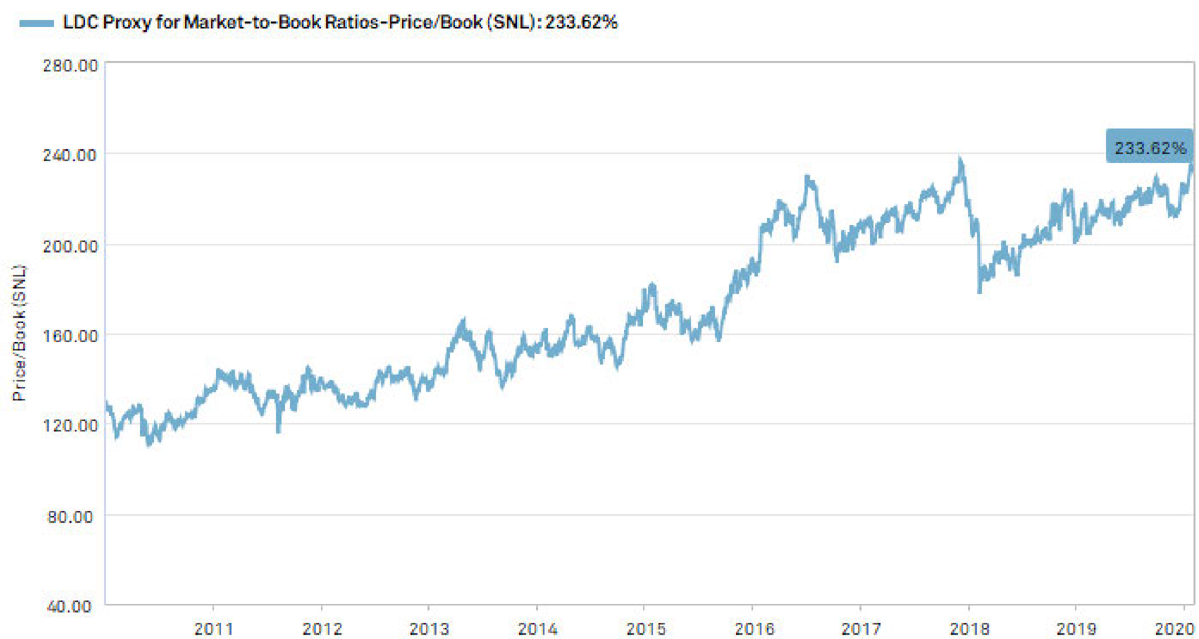


As this chart shows, the market-to-book ratios have recently increased to above 2-to-1, after trading as low as 1.5-to-1 in late 2023 into early 2024. Although not as high as the approximate 2.3-to-1 immediately before Covid-19, LDC market-to-book ratios are demonstrating a widening spread in earned ROEs over the COE.

Because publicly-traded utility companies typically have engaged in mergers and acquisitions, the book value of companies' common stocks may include an allowance for goodwill (purchase price over the book value of the assets). After deducting goodwill from the book value of the common stock, the market-to-book ratios for LDCs is approximately 2.5-to-1. These higher market-to-book ratios support both my position, and those of investors and financial advisors, that earned ROEs are higher than the COE.

Q. In your direct testimony, you cited Barclay's commentary/analysis that recognized that authorized ROEs did not decline along with the cost of capital since 2010.[54] Do LDC's price-to-book ("P/B") ratios over this period support Barclay's view?

A. Yes. See the following chart showing LDC's price-to-book ratios over the period 2010 through 2020:



As shown, the P/B ratios for the LDC group gradually expanded from 2010 through 2020 as the cost of capital declined, but authorized ROEs remained "sticky." This long-term trend is further evidence of the established financial principle that as companies expand their earnings margin over their COE, it causes their market-to-book ratios to increase. As it relates to utilities, this paradigm was more a function of maintaining authorized ROEs while their COE declined.

[54] Murray Direct, p. 14, l. 14 – p. 15, l. 2.

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Q. Ms. Bulkley claims that your multi-stage DCF analysis is less reliable than a constant-growth DCF analysis using equity analysts' projected long-term growth in EPS as the constant growth rate.[55] What is the basis of her position?

A. She testifies that because the utility industry is a mature industry, equity analysts' consensus projected long-term CAGR in EPS are likely to be consistent with an expected constant growth rate in perpetuity.

Q. In your experience reviewing and analyzing equity analyst research, have you ever discovered a utility equity analysis that assumes a utility's DPS will grow in perpetuity at the same rate as a projected 3-to-5-year CAGR in EPS?

A. No.

Q. In your experience reviewing and analyzing equity analyst research, what version of the DCF is used for purposes of estimating the intrinsic value of utility stock?

A. A multi-stage DCF or, more specifically, a multi-stage DDM (dividend discount model).

Q. Is Ms. Bulkley correct that equity analysts' projected 3-to-5-year CAGRs in EPS are stable over time?

A. No. For quarterly intervals since June 30, 2018, I reviewed consensus analysts' projected 3-to-5-year CAGRs in EPS for the companies in Ms. Bulkley's proxy group. The average low projected 3-to-5 year CAGRs in EPS for this period was 3.44% with the average high projected 3-to-5 year CAGRs in EPS was almost three times as high at 9.39%. Simply put, constant/perpetual growth rates should not change much over time.

Q. Is a perpetual growth rate of approximately 2.5% to 3.5% consistent with utility companies' rate base growth during periods of maintenance-level capital expenditures?

A. Yes. Before Ameren Missouri was able to elect PISA in 2018, Ameren Corp communicated to investors that its investment in Ameren Missouri was limited to

[55] *Id.,* p. 84, ln. 1 – p. 85, ln. 5.

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maintenance-level capex. Before Ameren Missouri elected PISA, its CAGR in rate base was in the range of 2.2% to 3% for the period 2010/2011 to 2019.[56]

Additionally, after the ICC's decision regarding AIC's multi-year rate plan for its electric utility operations, Ameren Corp now plans to invest a maintenance-level of capital expenditures in AIC's electric utility system. Ameren Corp now targets a 5-year CAGR in rate base of 2.3% for its AIC electric utility operations.[57]

Q. Ms. Bulkley suggests the perpetual growth rate in your multi-stage DCF analysis should be similar to expected long-term growth in the U.S. economy.[58] Do you agree?

A. No. The simplest way to illustrate the fallacy of Mr. Bulkley's suggestion that the LDC industry growth will converge to GDP growth in the long-term is to consider the impact of the appropriate application of this logic to the S&P 500 index. Because the S&P 500 index is considered a proxy for the U.S. stock market, it is logical that the expected long-term growth of the S&P 500 would be constrained by expected growth in GDP. However, because, on average, the companies in the S&P 500 tend to have better growth prospects than LDCs, the dividend payout ratio and the dividend yield is lower. This fact implies that the growth rate for LDCs should be lower than an aggregate growth rate, (*i.e.*, GDP) used for the U.S. market (*i.e.*, the S&P 500).

Adding Ms. Bulkley's suggested GDP growth rate of approximately 5.5% to her determination of a 1.54% dividend yield for the S&P 500[59] results in a market COE estimate of 7.04%. Because LDCs have a higher dividend yield due to a higher dividend payout ratio and lower growth expectations than the S&P 500, adding the same GDP growth rate of 5.50% to Ms. Bulkley's determination of an average 4.09% dividend yield in her "90-day Constant Growth DCF" analysis, results in a COE estimate of approximately 9.59%. These results are illogical based on the well-accepted and supported understanding that the regulated utility industry is the lowest-risk sector in the S&P 500.

[56] Case No. ER-2021-0240, David Murray Direct Testimony, p. 22, lines 13-20.
[57] "Powering a Reliable, Sustainable Tomorrow: Third Quarter 2024 Earnings," November 7, 2024, p. 13.
[58] Bulkley Rebuttal, p. 85, ln. 6 – p. 86, ln. 19.
[59] Bulkley Direct, p. 32, lns. 2-6.

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Q. Regardless of this disagreement, are there contradictions in her approach to estimating nominal GDP growth over the long-term?

A. Yes. Ms. Bulkley cites to several sources that provide projected inflation figures over the long-term.[60] However, instead of relying on the same source for projected sustainable growth in GDP over the long-term, she used historical GDP growth from 1929 to 2024 as a proxy for projected GDP growth.

Q. Which of Ms. Bulkley's sources also provide projected nominal GDP data?

A. The Energy Information Administration ("EIA"). The EIA directly estimates real GDP and the GDP Chain-Type Price Index that, when combined, provides a direct estimate of nominal GDP. For the period through 2050, EIA estimates a CAGR in nominal GDP of 4.25%.

Q. **

[60] Bulkley Rebuttal, Schedule AEB-R1, Attachment 9.
[61] *Id.*, p. 88, ln. 8 – p. 89, ln. 7.

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Q. How do you respond to Ms. Bulkley's criticism that your CAPM COE estimates underestimate the COE?

A. She not only disagrees with my view, but also Bank of America's ("BofA") view on a reasonable COE estimate under a higher long-term interest rate environment. BofA stated the following in an equity research report it published in October 2023, when long-term interest rates peaked in the fall of 2023:

> **On a spot basis with 9.5-9.6% after-tax authorized ROEs in 3Q23, this is meaningfully higher than the cost of equity from the capital asset pricing model for most utilities in the 8.5-9.0% range.** The 5% 30Yr US Treasury has compressed returns for utilities which have back-levered but we do not foresee a meaningful increase in allowed ROEs back above 10%. We continue to believe that California will not increase the allowed rate of return for the electric utilities due to the continuation of the extraordinary event from covid and the related policy responses.[62] (bold in the original).

Q. The above quote does not specify the variables such as beta and the market risk premium. Why do you claim that this information corroborates the reasonableness of your inputs to your CAPM analysis?

A. Because the end-result of BofA's estimates corroborate my COE estimates for the LDC industry, whether it's through my use of the CAPM, multi-stage DCF, or the simple bond-yield-plus-risk-premium ("BYPRP") methodology. Although my CAPM COE estimates were closer to 8% rather than 8.5% to 9.0%, 30-year United States Treasury yields were at 5% when BofA performed its CAPM analysis. At the time I performed my analysis, they were 34 basis points lower at approximately 4.66%. Therefore, assuming BofA applied similar assumptions (e.g. beta and market risk premium) in their CAPM analysis, as they did in October 2023, their COE estimates for the utility industry would still be less than 8.5% to 9.0%.

Q. Considering the fact that utilities' cost of equity increased since 2022, why would investors not expect authorized ROEs to increase as well?

A. As BofA's comments address, authorized ROEs are still "meaningfully" higher than the COE. If authorized ROEs are higher than utilities' COE, then utilities can create shareholder value by merely investing in its rate base and achieving a return over its cost of equity. If authorized ROEs are below the COE, which occurred in the early 1980s,

[62] Julien Dumoulin-Smith, et. al, "Utilities in a 5% Treasury World: Who has a plan to withstand the pain? 3Q Preview," Bank of America Securities, October 20, 2023.

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utility investment destroys shareholder value, which causes market-to-book ratios to be less than one.

Q. Ms. Bulkley testifies that the "rule of thumb" COE estimate you provide is too simplistic and inconsistent with other risk premiums Dr. Won used in past rate cases.[63] Can you provide the full context of the Chartered Financial Analyst ("CFA") Program curriculum which explains this reasonableness check?

A. Yes. The specific language from the CFA Program curriculum is as follows:

> 4.3.2 *Bond Yield Plus Risk Premium*
>
> For companies with publicly traded debt, the **bond yield plus risk premium method** [bold in original] provides a quick estimate of the cost of equity. The estimate is
>
> BYPRP cost of equity = YTM on the company's long-term debt + Risk premium
>
> The YTM on the company's long-term debt includes
>
> - a real interest rate and a premium for expected inflation, which are also factors embodied in a government bond yield; and
> - a default risk premium.
>
> The default risk premium captures factors such as profitability, the sensitivity of profitability to the business cycle, and leverage (operating and financial) that also affect the returns to equity. The risk premium in Equation 13 [above] is the premium that compensates for the additional risk of the equity issue compared with the debt issue (recognizing that debt has a prior claim on the cash flows of the company). In US markets, the typical risk premium added is 3%–4%, based on experience.[64]

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[63] Bulkley Rebuttal, p. 101, ln. 4 – p. 103, ln. 8.
[64] Refresher Reading, 2021 CFA Program, Level II, Reading 25, p. 35.

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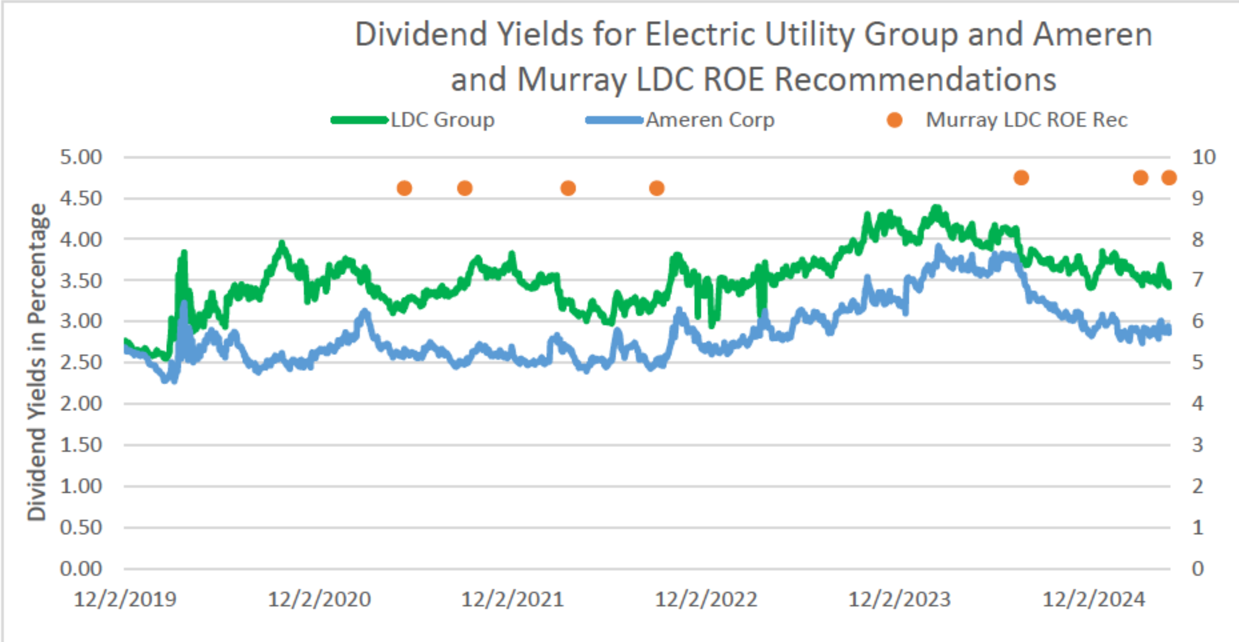
Q. Ms. Bulkley testifies that in past rate cases, Staff has recommended higher equity risk premiums to add to a company's or companies' own bond yield for purposes of this test of reasonableness.[65] Was Staff's suggested risk premiums of 4.0% to 6.0% based on the above-defined approach?

A. No. As I testified in Missouri American Water Company's 2020 rate case, Case No. WR-2020-0344, Staff added estimated market risk premiums, derived from studies comparing market returns to US Treasury Bond yields.[66] Because US Treasury Bond yields are lower than company-specific bond yields, mainly due to no default risk premium required on a US Treasury Bond, these higher risk premiums should not be applied to corporate bond yields. It is clear from the CFA Program curriculum that the 3% to 4% is based on a typical equity risk premium over a company's own bond yield.

Q. Ms. Bulkley provides a chart on page 78 of her rebuttal testimony where she compares your recommended ROEs to inflation and 30-year Treasury yields. What is your response?

A. A more appropriate comparison is to plot my recommended authorized ROEs for only LDC rate cases against my LDC group's dividend yields and Ameren Corp's dividend yields after the onset of Covid-19. That comparison follows:

[65] Bulkley Rebuttal, p. 101, ln. 16 – p. 102, ln. 11.
[66] Case No. WR-2020-0344, David Murray Rebuttal Testimony, p. 48, lns. 3-24.



Before Covid-19, there was a clear downward trend line for all utilities' dividend yields and, consequently, an upward trend line for P/E ratios. Because of this downward trend, in Spire Missouri's 2017 rate case, I tried to convince the Commission to authorize a 9.25% ROE, which was lower than the Commission's recent 9.5% authorized ROEs for Missouri's electric utilities, Ameren Missouri and Evergy Metro. Unfortunately, the Commission was not convinced, authorizing Spire Missouri an ROE of 9.8%. Instead, the Commission appeared convinced by evidence proffered that interest rates would increase because the Commission cited "anticipated increasing interest rates" to support its decision. However, long-term interest rates continued to decline for several years until 2022.

In light of the continued low cost of capital until 2022, I continued to attempt to convince the Commission to lower authorized ROEs to 9.25% for Missouri's large electric and natural gas utilities. The Commission authorized The Empire District Electric Company ("Empire") a 9.25% ROE in Case No. ER-2019-0374 and Spire Missouri a 9.37% ROE in Case No. GR-2021-0108. As the utility industries' COE continued to remain relatively low through 2022, I continued to recommend the Commission set LDC's ROEs at 9.25%.

However, after utility stocks contracted in 2023, causing dividend yields to increase, I increased my authorized ROE recommendations for Missouri's LDCs and electric utilities

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to 9.5% to recognize the increase in the COE. I did not recommend authorized ROEs be increased as much as the increase in the COE because before the increase in the COE, authorized ROEs were being set at a significant margin over the COE.

SUMMARY AND CONCLUSIONS

Q. Would you summarize your points in this surrebuttal testimony?

A. Yes. This case is not the first time Ameren Corp has tried to preserve a higher equity ratio at its regulated subsidiary following the passage of significant legislation that allowed for more favorable ratemaking. It is also not unique to compare the parent company's financing structure to that of its subsidiaries when evaluating a fair and reasonable ratemaking capital structure.

The Commission need look no further than its two neighboring states, Illinois and Kansas, for more examples. Illinois went as far as codifying a 50% ratemaking equity ratio into law, but not until after the ICC Staff stood its ground in arguing for a more reasonable common equity ratio than that shown in AIC's "independently" managed capital structure. Kansas required a cap on equity ratios for purposes of approving the merger of equals transaction between Great Plains Energy and Westar Energy, with the cap being adjusted downward if the new holding company used too much leverage. Although the ERSP that governed Evergy's Kansas subsidiaries recently expired, Evergy's most recent rate cases in Kansas resulted in parties settling on an implied ratemaking capital structure consisting of 50% common equity and 50% long-term debt. As it relates to Missouri's ability to limit excessive common equity ratios, it is up to this Commission to do so in context of this rate case. Limiting the utilities' common equity ratios will not cause a decline in Ameren Missouri's credit quality unless Ameren Corp refuses to offset this financial risk by reducing the amount of holding company debt in its capital structure.

The Commission should authorize Ameren Missouri a 9.5% ROE. While the cost of capital has increased since Ameren Missouri's 2021 natural gas distribution rate case, current LDC valuation levels are similar to electric utility valuation levels in 2015, when this

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Commission first deemed an approximate 9.5% ROE as reasonable for electric utility companies, including Ameren Missouri.

Q. Does this conclude your testimony?

A. Yes.

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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 Adjust Its Revenues for Natural Gas Service	)))	Case No. GR-2024-0369

AFFIDAVIT OF DAVID MURRAY

STATE OF MISSOURI)
) ss
COUNTY OF COLE)

David Murray, of lawful age and being first duly sworn, deposes and states:

1. My name is David Murray. I am a Utility Regulatory Manager for the Office of the Public Counsel.

2. Attached hereto and made a part hereof for all purposes is my surrebuttal testimony.

3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.

David Murray

David Murray
Utility Regulatory Manager

Subscribed and sworn to me this 30th day of April 2025.

TIFFANY HILDEBRAND
NOTARY PUBLIC - NOTARY SEAL
STATE OF MISSOURI
MY COMMISSION EXPIRES AUGUST 8, 2027
COLE COUNTY
COMMISSION #15637121

Tiffany Hildebrand

Tiffany Hildebrand
Notary Public

My Commission expires August 8, 2027.