

# Exhibit No. 331P

**Exhibit No.:** \_\_\_\_\_  
**Issue(s):** Rate of Return (ROR)/Capital Structure  
**Witness/Type of Exhibit:** Murray/Surrebuttal  
True-Up Direct  
**Sponsoring Party:** Public Counsel  
**Case No.:** ER-2022-0129 and ER-2022-0130

**SURREBUTTAL TESTIMONY  
TRUE-UP DIRECT TESTIMONY**

**OF**

**DAVID MURRAY**

Submitted on Behalf of the Office of the Public Counsel

**EVERGY METRO, INC. D/B/A  
EVERGY MISSOURI METRO  
AND  
EVERGY MISSOURI WEST, INC. D/B/A  
EVERGY MISSOURI WEST**

CASE NOS. ER-2022-0129 AND ER-2022-0130

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Denotes Confidential Information that has been redacted

August 16, 2022

**PUBLIC**

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**SURREBUTTAL AND  
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OF  
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EVERGY MISSOURI METRO  
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EVERGY MISSOURI WEST**

**CASE NOS. ER -2022-0129 AND ER-2022-0130**

1 **Q. Please state your name and business address.**

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

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

6 A. Yes.

7 **Q. What is the purposes of your true-up direct testimony?**

8 A. To update the cost of long-term debt through the true-up date for both Evergy Metro, Inc.  
9 (“Metro”) and Evergy Missouri West, Inc. (“MO West”). I also provide an updated cost  
10 of short-term debt for the scenario in which I recommend MO West’s ratemaking capital  
11 structure include short-term debt. Additionally, I analyzed the most recent financial  
12 statement information available for Evergy, Metro and MO West to determine if I should  
13 change my initial capital structure recommendation. Although I decided not to change my  
14 initial capital structure recommendation, my updated capital structure analysis supports the  
15 reasonableness of my recommended ratemaking capital structure for Metro and MO West.  
16 My discussion of this updated information is included throughout the entirety of this  
17 testimony.

1 **Q. To which witnesses' rebuttal testimonies will you reply as it relates to your surrebuttal**  
2 **testimony?**

3 A. Evergy's witness Ann E. Bulkley and Staff witness Seoung Joun Won's, PhD, rebuttal  
4 testimonies as it relates to my capital structure and return on common equity ("ROE")  
5 recommendation. Although Evergy witness Darrin R. Ives addresses capital structure in his  
6 rebuttal testimony, he did not provide much detail other than making blanket statements.  
7 Therefore, there is nothing substantive in his testimony for me to address.

8 **Q. How will you approach the presentation of your testimony?**

9 A. At times I will address both Dr. Won and Ms. Bulkley together when I respond to their  
10 similar arguments, or lack thereof. This mainly applies to each party's lack of response to  
11 my specific capital structure concerns related to MO West. However, when addressing  
12 separate and distinct arguments raised by each witness, I'll address these arguments by  
13 witness.

14 **TRUE-UP OF LONG-TERM DEBT AND SHORT-TERM DEBT COSTS**

15 **Q. What is Metro's and MO West's embedded cost of long-term debt through May 31,**  
16 **2022?**

17 A. According to Metro's and MO West's response to OPC Data Request No. 3038, each  
18 company's embedded cost of long-term debt is approximately 3.96%. Each company  
19 issues its own long-term debt to third-parties. Therefore, while the cost is coincidentally  
20 the same, each company's cost of long-term debt is based on their own separate long-term  
21 debt issuances.

22 **Q. Do you recommend Metro's and MO West's authorized ROR be set based on the**  
23 **3.96% embedded cost of long-term debt?**

24 A. Yes.

1 **Q. What is MO West’s cost of short-term debt as of the true-up date?**

2 A. 1.03% based on the weighted-average yield of commercial paper outstanding.<sup>1</sup>

3 **Q. What was MO West’s weighted average interest rate on its short-term borrowings as**  
4 **of June 30, 2022?**

5 A. 1.92%.

6 **Q. Why did the cost of short-term borrowings increase so quickly?**

7 A. Because the Federal Reserve’s (“Fed”) recent increases to the target Federal Funds (“Fed  
8 Funds”) rate directly impacts rates on commercial paper. The Fed increased the Fed Funds  
9 rate by 75 basis points on June 16, 2022. The Fed increased the Fed Funds rate by another  
10 75 basis points on July 28, 2022. 30-day A2/P2 commercial paper traded at an approximate  
11 2.65% yield in early August 2022.

12 **Q. If short-term debt is included in MO West’s ratemaking capital structure, what cost**  
13 **do you consider reasonable?**

14 A. The future path of short-term rates is difficult to predict. While investors still expect the  
15 Fed to increase the Fed Funds rates a few more times through mid-2023 to approximately  
16 3.5% to 3.75%,<sup>2</sup> investors also anticipate that the Fed will start reducing rates shortly  
17 thereafter if inflation is under control and higher short-term rates are too restrictive for the  
18 economy. If the Fed Funds rate reaches this level, then MO West’s commercial paper costs  
19 may reach approximately 3.9% at their peak. However, rates should only remain this high  
20 for a short period. Due to the uncertainty of the path of short-term rates, I recommend the  
21 Commission use the most recent known cost of commercial paper, which was  
22 approximately 2.65%.

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<sup>1</sup> Energy Response to OPC Data Request No. 3039.

<sup>2</sup> [Countdown to FOMC: CME FedWatch Tool \(cmegroup.com\)](https://www.cmegroup.com/tools-services/fomc-countdown-to-fomc)

1 **Q. Have you attached schedules to this testimony to show your updated ROR**  
2 **recommendations?**

3 A. Yes. See Schedule DM-S-1 for my updated ROR recommendation for Metro and MO  
4 West.

5 **CAPITAL STRUCTURE**

6 **Q. Have any witnesses addressed your direct testimony as it relates to MO West’s capital**  
7 **structure being supported by a significant amount and percentage of short-term debt,**  
8 **especially since February 2021 when MO West financed Winter Storm Uri (“Storm**  
9 **Uri”) costs?**

10 A. No.

11 **Q. Is this a circumstance that deserves close scrutiny in determining fair and reasonable**  
12 **capital costs assigned to MO West’s ratepayers?**

13 A. Yes. MO West had to raise significant amounts of capital to fund extraordinary costs  
14 related to Storm Uri. As I indicated in my direct testimony, MO West financed these  
15 extraordinary costs by issuing commercial paper and borrowing from Evergy’s internal  
16 money pool. In a concurrent proceeding, Case No. EF-2022-0155, MO West is seeking  
17 Commission authority to securitize Storm Uri costs. However, in that case, instead of  
18 requesting ratepayers pay financing costs consistent with the cost of the short-term debt  
19 MO West incurred to finance Storm Uri, it is requesting ratepayers pay a financing charge  
20 of 8.9%, which not only includes an ROE of 9.5%, but also an allowance for taxes on this  
21 ROE. To be clear, MO West is requesting its shareholders be compensated for funding  
22 Storm Uri costs, although they **did not** finance Storm Uri. Even if shareholder funds were  
23 needed to provide liquidity to fund these extraordinary costs, this certainly should not be  
24 the controlling factor as to a fair and reasonable financing charge allowed to fund operating  
25 costs. While shareholders certainly deserve consideration for financing potential value-  
26 added investment, such as plant and equipment, the same should not hold true for financing  
27 operating costs.

1 **Q. Which of MO West’s affiliates has loaned it funds through Evergy’s internal money**  
2 **pool for purposes of assisting with financing of Storm Uri costs?**

3 A. Metro.

4 **Q. If MO West ratepayers pay an 8.9% financing charge for Storm Uri costs, should**  
5 **Metro receive an 8.9% return on the funds it loaned to the money pool?**

6 A. Yes.

7 **Q. How much capital has Metro loaned MO West through the money pool since Storm**  
8 **Uri?**

9 A. An average monthly outstanding balance of around \$125 million since April 2021. It has  
10 ranged from a low of \$6.7 million in April 2021 to a high of \$255 million in November  
11 2021.

12 **Q. How much interest was credited to Metro for the internal money pool loans for this**  
13 **period?**

14 A. \$212,653.

15 **Q. If Metro were allowed to collect the 8.9% ROR requested by MO West to finance**  
16 **Storm Uri costs, how much should Metro be credited for the capital it transferred to**  
17 **MO West?**

18 A. \$12,330,439.

19 **Q. What carrying cost rates did Staff and MO West agree to in their Stipulation and**  
20 **Agreement (S&A) in Case No. EF-2022-0155?**

21 A. 0.20% for the first six months and then a 5.06% cost of long-term debt until the securitized  
22 bonds are issued (estimated to occur in January 2023).



1 **Q. How much additional revenues would Metro have received through May 2022 if MO**  
2 **West paid interest based on MO West's embedded cost of long-term debt at June 30,**  
3 **2018?**

4 A. \$4.9 million through May 2022.

5 **Q. Are revenues Metro receives through its money pool loans included in Metro's**  
6 **revenue requirement?**

7 A. No. According to Evergy's response to OPC Data Request No. 3042, interest received  
8 from loans to Evergy's money pool are not included in the company's revenues (see  
9 Schedule DM-S-2).

10 **Q. If MO West customers are required to pay an 8.9% ROR for financing of Storm Uri**  
11 **costs, should Metro's revenues reflect such?**

12 A. Yes. Metro's revenues should be increased by \$4.9 million, which would cause a \$4.9  
13 million reduction to its revenue requirement.

14 **Q. Does MO West also borrow directly from commercial paper markets?**

15 A. Yes.

16 **Q. For the period March 2021 through May 2022, on average, what percentage of MO**  
17 **West's CWIP and Storm Uri balances have been supported by commercial paper and**  
18 **money pool borrowings?**

19 A. 89%.

20 **Q. What is the proportion of average CWIP balances to average short-term debt**  
21 **balances for the period March 2021 through May 2022?**

22 A. 42.65%.

1 **Q. How should the remaining 57.35% of short-term debt be considered for purposes of**  
2 **developing fair and reasonable rates for MO West?**

3 A. The first and best option is to capture these costs in Case No. EF-2022-0155 (the  
4 securitization case) by using MO West's cost of short-term debt to determine fair and  
5 reasonable carrying charges included in the final amount to be securitized. However, if  
6 short-term debt is not captured in the securitization case, then this short-term debt should  
7 be considered for purposes of setting MO West's allowed ROR.

8 **Q. Did you analyze more recent financial information to determine whether you should**  
9 **change your recommended ratemaking capital structures in these cases?**

10 A. Yes.

11 **Q. Has Evergy released financial information through June 30, 2022, which is one month**  
12 **after the true-up dated of May 31, 2022?**

13 A. Yes.

14 **Q. Did you analyze the more recent information to help inform your recommended**  
15 **ratemaking capital structure and resulting ROR?**

16 A. Yes.

17 **Q. Has your review and analysis of this financial information caused you to change your**  
18 **recommended ratemaking capital structure for Metro or MO West?**

19 A. No.

20 **Q. If you had changed any of your recommended ratemaking capital structures due to**  
21 **your consideration of additional and more recent financial information, which**  
22 **recommendation would you change?**

23 A. My recommendation for MO West, but only for the second scenario, which is premised on  
24 the assumption that short-term debt rates are not used for purposes of calculating carrying

1 costs in MO West’s current securitization case, Case No. EF-2022-0155. As can be seen  
2 in Schedules DM-S-3, pages 4-7, MO West’s use of short-term debt in excess of CWIP has  
3 been increasing since June 30, 2020. Although not shown on the schedules, at June 30,  
4 2022, MO West outstanding short-term debt balance was at its highest level of \$690.5  
5 million.<sup>3</sup> Of course for the period since February 2021, most of the short-term debt in  
6 excess of CWIP is explained by MO West’s financing Storm Uri costs.

7 **Q. Considering the difficulties of predicting short-term debt rates and the likelihood that**  
8 **MO West will reduce its short-term debt outstanding after it issues securitized debt,**  
9 **what do you consider a reasonable and fair alternative to including short-term debt**  
10 **in MO West’s ratemaking capital structure?**

11 A. Considering the nuances created by the financing of Storm Uri, as well as the distortion on  
12 Metro’s books caused by Evergy’s increased use of holding company commercial paper, a  
13 reasonable solution to these issues is to require all of MO West’s and Metro’s CWIP to be  
14 capitalized by a short-term debt rate. This will allow ratepayers to receive credit for each  
15 company’s use or expected use of short-term financing and allow a more reasonable  
16 allowance for funds used during construction (“AFUDC”) rate as well as the ability to  
17 capture the actual changes to the cost of short-term debt in between rate cases.

18 **ANN E. BULKLEY’S REBUTTAL TESTIMONY**

19 **Q. Ms. Bulkley indicates that your recommend ratemaking capital structures for MO**  
20 **West and Metro are premised on two different bases.<sup>4</sup> Is she correct?**

21 A. No. If the Commission captures MO West’s use of short-term debt to support Storm Uri  
22 assets in the concurrent securitization case, I am recommending the same ratemaking  
23 capital structure for MO West and Metro. My recommendation is based on my analysis of  
24 the amount of leverage contained in Evergy’s consolidated capital structure, which through  
25 June 30, 2022, was even more leveraged than quarterly periods through December 31,

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<sup>3</sup> Evergy’s SEC Form 10-Q Filing, June 30, 2022, p. 39.

<sup>4</sup> Bulkley Rebuttal, p. 12, lns. 7-10.

1 2021. Ms. Bulkley incorrectly states that the basis for my MO West capital structure  
2 recommendation is a provision from the Kansas Corporation Commission’s (“KCC”)  
3 approval of the Westar Inc. and Great Plains Energy merger. While I did identify the 50%  
4 common equity ratio used for the KCC’s approved Earnings Review and Sharing Plan  
5 (“ERSP”) as a potential upper limit for a reasonable ratemaking capital structure for MO  
6 West in my MO West direct testimony, I indicated the same in my Metro direct testimony.  
7 Perhaps, this was an oversight on her part due to the complications and confusion of filing  
8 similar, but slightly different testimonies for each company. If so, I sympathize.

9 **Q. Ms. Bulkley dismisses the relevance of the 50% common equity ratio established for**  
10 **purposes of ERSP because it “had no effect on the company’s rates, and in no way**  
11 **limited the company’s actual capital structure.”<sup>5</sup> Do you agree with Ms. Bulkley’s**  
12 **assessment?**

13 A. No. Limiting Evergy Kansas Central’s common equity ratio to 50% has a direct impact on  
14 the amount of earnings the company can retain for its shareholders compared to that which  
15 it must share with ratepayers. While the company’s rates may not change, the economic  
16 impact of limiting the company’s earnings is the same. Using a simplified example of \$1  
17 billion in rate base and a 9.3% ROE, if the Company’s ERSP is based on a 50% common  
18 equity ratio, the trigger for sharing earnings with ratepayers is a net income of \$46.5  
19 million. If the ERSP was still premised on a 51% common equity ratio, the trigger for  
20 sharing earnings with ratepayers is net income of \$47.43 million, a difference of \$930  
21 thousand. Therefore, the limit on the common equity ratio has a real economic impact on  
22 ratepayers and shareholders.

23 As far as a limitation on the company’s actual capital structure, Evergy could certainly  
24 manage Evergy Kansas Central’s common equity ratio to a higher or lower ratio, but that’s  
25 not the point. The point of the ERSP was to set the common equity ratio for purposes of  
26 determining whether Evergy Kansas Central should be required to share excess earnings

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<sup>5</sup> *Id.*, p. 13, lns.6-7.

1 with its ratepayers. For this purpose, a lower common equity ratio applied to a 9.3% ROE  
2 results in a higher amount of sharing with ratepayers.

3 **Q. Ms. Bulkley argues that your more leveraged capital structure recommendation is**  
4 **not supported by reduced business risk associated with MO West’s and Metro’s**  
5 **election of PISA. She claims that both companies “utilize PISA for the timely**  
6 **recovery of some capital expenditures between rate cases.”<sup>6</sup> Does Ms. Bulkley**  
7 **quantify her characterization of “some?”**

8 A. No.

9 **Q. When Evergy announced its Sustainability Transformation Plan (“STP”) after the**  
10 **conclusion of its strategic review of pursuing a merger or continuing as a standalone**  
11 **company, what percentage of Evergy’s announced capital expenditures for Missouri**  
12 **were expected to be PISA eligible?**

13 A. 88%. Evergy indicated that \$2.9 billion of the planned \$3.9 billion in capital expenditures  
14 for its Missouri utilities would be PISA eligible.<sup>7</sup>

15 **Q. Ms. Bulkley argues that MO West’s and Metro’s requested capital structures should**  
16 **be compared against other current average authorized equity ratios to determine if**  
17 **the various parties’ recommended ratemaking capital structures are reasonable.**  
18 **Considering the significant changes in Evergy’s issuance of holding company short-**  
19 **term debt, which has recently been used to infuse common equity into MO West, do**  
20 **you consider MO West’s and Metro’s past requested equity ratios under Great Plains**  
21 **Energy to be a better barometer of reasonableness?**

22 A. Yes. In many instances, MO West and Metro itself requested ratemaking common equity  
23 ratios below 50%. In rate cases prior to 2016, MO West and Metro requested common  
24 equity ratios similar to that of its publicly-traded parent company, Great Plains Energy,  
25 which, because its capital structure was a function of third-party capital transactions, it

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<sup>6</sup> *Id.*, p. 20, lns. 9-11

<sup>7</sup> Sustainability Transformation Plan, August 5, 2020, p. 8.

1 could not easily manipulate to hit ratemaking targets. Consequently, the common equity  
2 ratios requested by Metro and MO West ranged from 46.29% in their 2010 rate cases<sup>8</sup> to  
3 52.56% in their 2012 rate cases.<sup>9</sup> In its 2014 rate case, Metro requested a common equity  
4 ratio of 50.09%.<sup>10</sup>

5 Considering the decline in business risk for Missouri's electric utilities since the passage  
6 of PISA and the Securitization Law, it is not rational to expect MO West and Metro to need  
7 to maintain an equity ratio higher than that which GPE typically maintained (slightly below  
8 50%) over the period between 2013 until 2016, right before it issued approximately \$3.2  
9 billion in preferred and common equity in anticipating of acquiring Westar.

10 **Q. Ms. Bulkley claims that you abandoned/discarded your COE estimates for purposes**  
11 **of your recommended allowed ROE range of 8.5% to 9.50%, point recommendation**  
12 **of 9.0%.<sup>11</sup> Is this an accurate representation of your testimony?**

13 A. No. My recommended authorized ROE of 9.0% takes into consideration many different  
14 factors. A fundamental principle of shareholder value creation is for a company to invest  
15 in projects that allow the company earn at least its cost of capital. An allowed ROE of  
16 9.0% allows for a margin of approximately 150 to 200 basis points over my estimate of  
17 Metro and MO West's COE in the range of 7.0% to 7.5%. Investors have become  
18 accustomed to regulators allowing utility companies returns that are higher than their cost  
19 of capital. In fact, some investors, such as Evercore ISI, use investment models that assume  
20 that regulators currently allow an ROE to COE spread of approximately 440 basis points  
21 (9.75% ROE – 5.35% COE), but will eventually reduce the spread to a range of 225 to 285  
22 basis points as either the COE increases, the allowed ROEs decrease or a combination of  
23 both.<sup>12</sup>

<sup>8</sup> Case Nos. ER-2010-0355 and ER-2010-0356.

<sup>9</sup> Case Nos. ER-2012-0174 and ER-2012-0175.

<sup>10</sup> Case No. ER-2014-0370.

<sup>11</sup> Bulkley Rebuttal, p. 4, lns. 4-8, p. 13, lns. 17-19 and p. 51, lns. 7-9.

<sup>12</sup> Durgesh Chopra, et. al., "Q2 Earnings Season in Final Innings" Evercore ISI, August 7, 2022, p. 5.

1 The fact that the COE for utilities is this low establishes the reasonableness of my  
2 recommended authorized ROE, which actually allows Evergy to increase shareholder value  
3 above the classic economically efficient amount, which at least theoretically should be no  
4 greater than the value created from earning a return consistent with the cost of capital.  
5 Regardless, my determination that the COE is much lower than Metro's last authorized  
6 ROE of 9.5% supports reducing Metro's and MO West's authorized ROE. However, I also  
7 understand from past Commission decisions that the Commission has set a zone of  
8 reasonableness ("ZOR") that has generally been 100 basis points (1%) above and below  
9 recent average authorized ROEs. Recent average authorized ROEs have been  
10 approximately 9.4%.<sup>13</sup> Therefore, the low-end of my recommended ROE range, 8.5%, is  
11 within the Commission's expressed ZOR.

12 **Q. Ms. Bulkley suggests that because you recommend an authorized ROE higher than**  
13 **your COE estimates, you should have reconsidered the validity of the inputs and**  
14 **assumptions you used in your COE analysis.<sup>14</sup> What is Ms. Bulkley's underlying**  
15 **assumption for her criticism?**

16 A. Ms. Bulkley assumes commission authorized ROEs are equal to the COE. As I have  
17 demonstrated through numerous practical and internal company documents and analysis,  
18 the COE is lower than authorized ROEs. However, recognizing that commissions,  
19 including this Commission, are resistant to reducing authorized ROEs to much below 9%,  
20 I factor such into my final ROE recommendation.

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<sup>13</sup> S&P Global Market Intelligence, "Major energy rate case decisions in the US – January-June 2022," July 27, 2022.

<sup>14</sup> Bulkley Rebuttal, p. 23, ll. 17-20.

1 **Q. Ms. Bulkley indicates you have presented no evidence to support your claim that**  
2 **utility companies' COE is lower than authorized ROEs, but rather it is your "own**  
3 **personal opinion that authorized ROEs are greater than the cost of equity..."<sup>15</sup> Did**  
4 **you attach evidence to your direct testimony to corroborate your position?**

5 A. Yes. First, my COE analysis is evidence that the COE is lower than authorized ROEs.  
6 Second, I cited several equity analysts' reports that indicate the COE is lower than  
7 authorized ROEs. Finally, and most damaging to Ms. Bulkley's credibility as an Evergy  
8 witness, Evergy's own financial advisors, Morgan Stanley and Goldman Sachs, estimated  
9 a COE of below \*\* \_\_ \*\* for purposes of discounting future projected cash flows under  
10 Evergy's STP. Morgan Stanley and Goldman Sachs estimated a COE that is \*\* \_\_ \*\*  
11 that estimated by Ms. Bulkley.

12 **Q. Based on these practical and consequential use of COE estimates, do you have any**  
13 **suggestions for Ms. Bulkley for purposes of testing the reasonableness of her inputs**  
14 **and assumptions?**

15 A Yes. I'd suggest she review the specific utility investor reports I reviewed to determine the  
16 assumptions they used when valuing utility stocks. I also suggest that she review the same  
17 Evergy internal materials I reviewed as it relates to estimating the best path forward to  
18 create shareholder value for Evergy's shareholders.

19 **Q. Ms. Bulkley indicates that your multi-stage DCF results are too low to be reasonable**  
20 **and are not reflective of the COE.<sup>16</sup> What is the basis for her position?**

21 A. Her position is based on her claim that the COE cannot be this low because "not a single  
22 jurisdiction has authorized an ROE as low as the results of Mr. Murray's Multi-Stage DCF  
23 model."<sup>17</sup> Again, Ms. Bulkley and I disagree as to relevant information to test the  
24 reasonableness of our COE estimates. She appears to consider regulatory allowed ROEs  
25 as the "stamp of approval" as to COE estimates for utility companies. Investors have long

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<sup>15</sup> *Id.*, p. 77, lns. 1-4.

<sup>16</sup> *Id.*, p. 79, lns. 9-10.

<sup>17</sup> *Id.*, lns. 10-11.



1 wondered why authorized ROEs had not declined more to reduce the allowed ROE-to-  
2 COE spread. Investors more or less chalked it up to “stickiness.”<sup>18</sup> This “stickiness”  
3 causes circularity in authorized ROEs throughout the country to the extent that regulators  
4 accept arguments similar to Ms. Bulkley’s. However, investors have also expressed the  
5 view that because commissions did not lower authorized ROEs along with the significant  
6 decline in the costs of capital, they also don’t expect commissions to start increasing  
7 authorized ROEs at the first hint of increases in interest rates.

8 **Q. Ms. Bulkley and Dr. Won suggest that I am not recognizing the increased cost of**  
9 **capital to utilities caused by increases in interest rates. Are you ignoring these factors**  
10 **in your cost of capital analysis?**

11 A. No. I agree with Ms. Bulkley and Dr. Won that typically, interest rates and utility stock  
12 prices are negatively correlated. However, recent capital market conditions have not been  
13 typical. Rather than a negative correlation to interest rates, utility stocks have recently  
14 exhibited a strong positive correlation to interest rates. As I explained in my rebuttal  
15 testimony, this could be due to a couple of factors in the current market environment. First,  
16 utility stock prices did not increase during the significant decrease in interest rates during  
17 2020 and 2021, which certainly implies that investors in utility stocks did not expect long-  
18 term rates to remain low. Second, investors’ fear of a recession caused by the Fed’s  
19 aggressive fighting of inflation through sharp increases in the Fed Funds rate outweighs  
20 the attraction of higher bond yields as compared to the defensive characteristics of utility  
21 stocks.

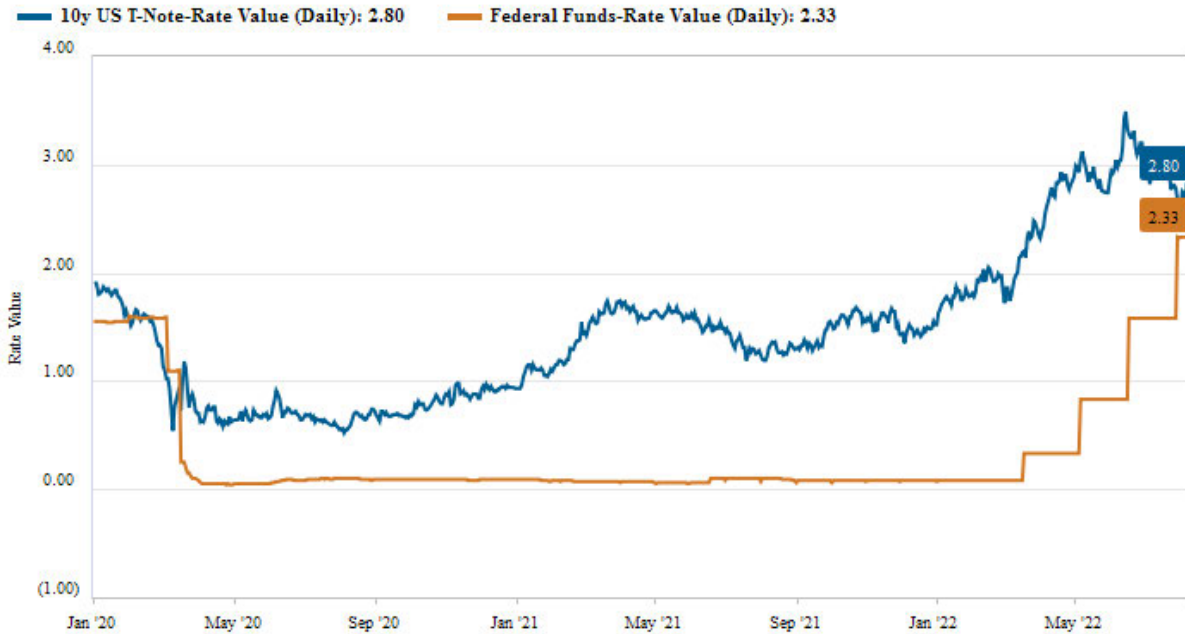
22 **Q. Have long-term interest rates continued to increase in conjunction with the Fed**  
23 **increasing the Fed Funds target rate?**

24 A. No. The below chart shows the effective yield on the Fed Funds rate as compared to the  
25 10-year United States Treasury (“UST”) yield. As can be seen, long-term yields have  
26 declined since they peaked mid-June 2022. This is consistent with investors’ view that

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<sup>18</sup> Neil Kalton, Sarah Akers, Jonathan Reeder, David Welkener, “Utility and Infrastructure Outlook 2020 (And Beyond),” January 8, 2020, Wells Fargo

1 while the Fed may raise the Fed Funds rate aggressively over the next year or so, it may be  
2 required to lower them quickly if the economy enters a recession.



3  
4 **Q. Will utility stock prices decline in the future, if interest rates should resume their**  
5 **upward trajectory as suggested by Ms. Bulkley?**<sup>19</sup>

6 A. I don't know. Obviously interest rates had already increased without a corresponding  
7 decrease in utility stock prices. As shown in the above graph, since 10-year UST yields hit  
8 their recent high of 3.5% in June 2022, they have declined to 2.80%.

9 **Q. Do current bond prices provide an unbiased view of investors' expectations of future**  
10 **interest rates?**

11 A. Yes. This is consistent with the random walk theory which dictates that no investor has  
12 superior insight as to the likely path of securities' prices (which includes interest rates on  
13 bonds), and any corresponding superior return that can be achieved from having this  
14 foresight. Consequently, current yields-to-maturity (*i.e.* interest rates) are the best

<sup>19</sup> *Id.*, p. 80, lns. 13-14.

1 predictor of subsequent returns. John C. Bogle's, founder of Vanguard Group, view  
2 regarding expected returns on bonds was expressed as follows in a 2016 Wall Street Journal  
3 article:

4 As for bonds, Mr. Bogle has found that essentially all you need to know is  
5 the yield to maturity, or the implied interest rate that makes the present value  
6 of all of a bond's future cash flows equal to its current market price.  
7 Analyzing 10-year periods back to 1906, he found that at least 90% of the  
8 subsequent return on bonds could be explained by their initial yields; capital  
9 gains and losses barely registered. So, with the Barclays U.S. Aggregate  
10 index of government and corporate bonds yielding 2.6%, that's the baseline  
11 expectation.<sup>20</sup>

12 Mr. Bogle is best known for his advocacy of passive investing, hence his creation of low-  
13 cost, passive index funds at Vanguard. Mr. Bogle's view is consistent with the fundamental  
14 assumptions underlying cost of capital models, such as the DCF and CAPM, which is that  
15 market prices reflect all known and public information, which includes possible changes  
16 in interest rates and economic factors. Because utility ROR witnesses should be attempting  
17 to estimate the market cost of capital, which is based on current market prices, not  
18 speculative future prices, the foundation of our analysis should be similar to Mr. Bogle's  
19 view.

20 **Q. Can the Commission derive useful information from Ms. Bulkley's testimony to**  
21 **support the reasonableness of an authorized ROE of no higher than 9.25%?**

22 **A.** Yes. Ms. Bulkley freely admits that higher utility stock valuations are consistent with a  
23 low cost of equity. For example, she indicates the following on page 80 of her rebuttal  
24 testimony:

25 As interest rates increase, which is expected over the near term, the  
26 share prices of utility stocks will decline. A decline in share prices  
27 will result in an increase in the cost of equity estimate of the DCF  
28 model.<sup>21</sup>

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<sup>20</sup> Jason Zweig, "This Simple Was Is the Best Way to Predict the Market," *Wall Street Journal*, January 5, 2016.

<sup>21</sup> *Id.*, p. 80, lns. 13-15.

1           Therefore, the Commission should simply ignore Ms. Bulkley’s speculation about potential  
2           future market prices, but recognize the simple and fairly straightforward understanding that  
3           recent sustained higher valuations of electric utility stocks (around 20x P/E) despite  
4           increases in interest rates, supports at least maintaining authorized ROEs in the lower 9%  
5           range.

6           **Q.    Ms. Bulkley maintains that your terminal growth rate of 2.5% to 3.5% in your multi-**  
7           **stage DCF analysis is “not consistent with the stock prices that he [me] relies on to**  
8           **calculate his multi-stage DCF model.”<sup>22</sup> What does she mean?**

9           A.    Ms. Bulkley believes that because projected long-term (3-to-5-year) compound annual  
10           growth rates (“CAGR”) in earnings per share (“EPS”) averaged around 5% to 6% for the  
11           electric utility industry, that investors also expect electric utilities’ dividends per share  
12           (“DPS”) to grow in perpetuity at the same rate. This is not true. Most utility sell-side  
13           equity analysts only use projected CAGR in EPS for purposes of determining a relative  
14           P/E target multiple as compared to the industry average. For example, if an electric utility  
15           company has top quartile expected growth in EPS over the next five years, they may assign  
16           a 10% premium to the industry average P/E ratio to determine a target price. However,  
17           investors do not use a long-term projected CAGR in EPS for purposes of performing an  
18           absolute valuation analysis, such as a DCF (more specifically defined as a dividend  
19           discount model) analysis. For purposes of performing an absolute valuation analysis such  
20           as a DCF, investors use a perpetual growth rate much lower than current projected long-  
21           term CAGR in EPS.

22           **Q.    How do you respond to Ms. Bulkley’s criticism that your CAPM COE estimates are**  
23           **mis-specified due to market risk premium estimates of 5.5% to 6.0%?**

24           A.    My market risk premium estimates are corroborated by Evergy’s own financial advisors,  
25           Morgan Stanley and Goldman Sachs. They used market risk premium estimates of \*\*  
26           \_\_\_\_\_ \*\* (Goldman Sachs) and \*\* \_\_\_\_\_ \*\* (Morgan Stanley).

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<sup>22</sup> *Id.*, p. 82, lns. 11-12.

1 **Q. What is your response to Ms. Bulkley’s use of market returns for the period 2009**  
2 **through 2020 to refute the 8.5% to 8.94% implied market returns in your CAPM**  
3 **analysis?**

4 A. This is a glaring example of why using selective short-periods of achieved returns to predict  
5 future returns is misguided. To make matters worse, not only did Ms. Bulkley use a  
6 relatively short-period to determine required returns over an infinite period, she captured  
7 achieved returns subsequent to the United States capital markets reaching their nadir on  
8 March 9, 2009. The primary driver for outsized market returns over the past decade has  
9 been the Fed’s easy monetary policies rather than strong economic growth. This is best  
10 understood by also evaluating utility stock and corporate bond returns over the same  
11 period. Capital gains in fixed-income (*i.e.* bonds) securities are not caused by growth  
12 because bond coupons are constant. Therefore, the primary driver of recent total returns  
13 on bonds has been the change in average level of long-term interest rates. As can be seen  
14 in the below expanded table, approximately half of long-term government bonds total  
15 returns are due to capital gains as compared to income returns (*i.e.* the payment of  
16 coupons). Again, this is not due to growth in coupon payments, but rather a decline in  
17 interest rates, which causes bonds issued at higher coupons to be worth more due to a lower  
18 cost of capital.

Year	Large Company Stock	Long-Term US Government Bond Total Return	Long-Term US Govt. Return from Income	Long-Term US Govt. Return from Capital Gains
2009	26.46%	-14.90%	3.47%	-18.25%
2010	15.06%	10.14%	4.25%	5.89%
2011	2.11%	27.10%	3.82%	22.62%
2012	16.00%	3.43%	2.46%	0.95%
2013	32.39%	-12.78%	2.88%	-15.70%
2014	13.69%	24.71%	3.41%	20.93%
2015	1.38%	-0.65%	2.47%	-3.11%
2016	11.96%	1.75%	2.30%	-0.40%
2017	21.83%	6.24%	2.67%	3.51%
2018	-4.38%	-0.57%	2.82%	-3.50%
2019	31.49%	12.16%	2.55%	9.53%
2020	18.40%	16.65%	1.42%	15.12%
<b>Arithmetic Average</b>	15.53%	6.11%	2.88%	3.13%
<b>Variance</b>	1.36%	1.70%	0.01%	1.64%
<b>Geometric Average</b>	14.98%	5.37%	2.87%	2.39%

**Percent of Total Long-Term Govt. Bond Return from Capital Gains:**

Arithmetic	51.29%
Geometric	44.53%

1  
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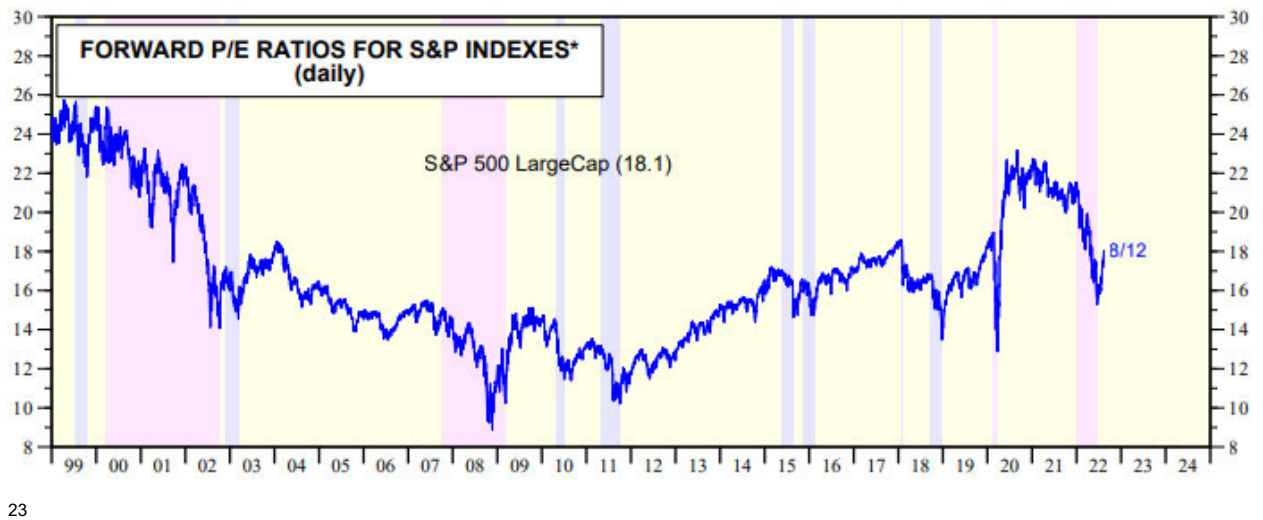
Therefore, the decline in the cost of capital has caused investors to achieve returns higher than they expected. Ms. Bulkley’s suggestions that outsized capital gains (the market is more expensive to investors and cheaper for stock issuers) supports a higher cost of capital is completely counterintuitive to the fact that as P/E ratios increase, the stock market becomes more expensive to investors (lower required returns) and cheaper for those issuing stock (*i.e.* companies).

Another illustrative example of the fallacy of Ms. Bulkley’s equating the last twelve years of large company stock returns with an estimate of required returns is to observe the 12

1 years of large company stock returns before the 12-year period Ms. Bulkley analyzed. The  
2 returns are shown in the following table:

Year	Large Company Stock
1997	33.36%
1998	28.58%
1999	21.04%
2000	-9.10%
2001	-11.89%
2002	-22.10%
2003	28.68%
2004	10.88%
2005	4.91%
2006	15.79%
2007	5.49%
2008	-37.00%
<b>Arithmetic Average</b>	5.72%
<b>Variance</b>	4.82%
<b>Geometric Average</b>	3.39%

3  
4 Following Ms. Bulkley’s logic of using a 12-year period of realized returns on the S&P  
5 500 to project investors required returns going forward, the above realized returns imply  
6 that investors were willing to invest in the S&P 500, when risk aversion was near its peak,  
7 for a required a return of 5.72%. Because 30-year UST yields were approximately 3% at  
8 the end of 2008, this analysis would imply that investors only required a market risk  
9 premium of 2.72% to invest in the S&P 500. As can be seen in the below graph, the S&P  
10 S&P 500 P/E ratios at that time were only around 10x, whereas at the end of 2020 (the  
11 ending period in Ms. Bulkley’s analysis), the S&P 500 was trading at a P/E ratio of  
12 approximately 22x to 23x. It is completely illogical to project higher risk premiums when  
13 valuation levels are higher as compared to when they are lower.



### WON'S REBUTTAL TESTIMONY

**Q. Staff witness Dr. Won criticizes your recommended ROE of 9.0% because he claims it does not properly reflect the increased COE since the Commission determined an authorized ROE of 9.25% was reasonable for Empire. How do you respond?**

A. I agree that the COE increased since I performed my COE analysis for Empire's and Ameren Missouri's rate cases in 2019. In those cases, I had estimated the electric utility industry's COE was in the range 5.5% to 6.5%. However, as I explained in those cases, electric utility stock valuation levels were then at all-time highs. Naturally, this translated into very low COE estimates. While it was certainly my opinion that this justified the Commission's consideration to lower Missouri's electric utilities' authorized ROEs, I also recognized potential market shock if they were reduced dramatically in one fell swoop.

**Q. Dr. Won suggests that because the COE has increased since the Empire rate case, this supports authorizing Metro and MO West an ROE of 9.62%. What is the problem with Dr. Won's logic?**

A. It is literally too short-sighted. It fails to consider the longer-term trend in Metro's and MO West's cost of capital both due to macro trends and more investor friendly rate making

<sup>23</sup> Dr. Edward Yardeni, "Stock Market Briefing: Selected P/E Ratios," Yardeni Research Inc., August 12, 2022.



1 mechanisms now allowed in Missouri. Metro's current authorized ROE of 9.5% was  
2 decided in Case No. ER-2016-0285, and did not change from Metro's authorized ROE of  
3 9.5% in Case No. ER-2014-0370. Although the cost of capital was low in 2015 compared  
4 to the historical standards at that time, it pales in comparison to more recent capital markets.  
5 Additionally, Metro's and MO West's business risk has declined over this period. Because  
6 my rebuttal testimony already provides my illustrative (charts of electric utility P/E ratios  
7 since 2014 with focus on certain periods since 2014) and written explanation of why Dr.  
8 Won and I disagree as to the reasonableness of an ROE above 9.5%, I will not repeat these  
9 same points in responding to Dr. Won's rebuttal testimony.

10 **Q. Does Dr. Won dispute your testimony that the Commission explicitly decided Metro's**  
11 **and MO West's ROE in 2015?**

12 A. Yes. He claims that the "Commission approved a settled 9.5% ROE" in 2015.<sup>24</sup>

13 **Q. Did the Commission authorize a 9.5% ROE in Metro's 2014 rate case, which was**  
14 **decided in 2015?**

15 A. Yes. See page 22 of the Commission's September 2, 2015 Report and Order in Case No.  
16 ER-2014-0370.

17 **Q. Were you correct in stating that the Commission had explicitly decided MO West's**  
18 **authorized ROE in 2015?**

19 A. No. MO West did not file a rate case in 2014.

20 **Q. What about the 2016 rate cases?**

21 A. Metro's rate case, Case No. ER-2016-0285, was also litigated and the Commission's  
22 Report and Order deemed a 9.5% ROE as fair and reasonable. However, MO West's rate  
23 case, Case No. ER-2016-0156 was settled, with the settlement specifying a range of 9.5%  
24 to 9.75%.

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<sup>24</sup> Won Rebuttal, p. 26, ll. 9-12.

1 **Q. Dr. Won claims that you insist that current authorized ROEs have declined compared**  
2 **to 2015.<sup>25</sup> Did your direct testimony focus on changes in authorized ROEs since 2015?**

3 A. No. My direct testimony focused on the general decline in the COE since 2015. Because  
4 this Commission's authorized ROE in 2015 (not average authorized ROEs in other  
5 jurisdictions) was 9.5% for its major electric utilities, I consider the long-term decline in  
6 the COE since this period to support a reduction to this Commission's previous  
7 determination of 9.5% as a fair and reasonable authorized ROE. Although I did not analyze  
8 general authorized ROEs in 2015 in my direct testimony, I note that in those 2015  
9 decisions, the Commission considered average authorized returns at that time before  
10 deciding a 9.5% ROE was fair and reasonable.

11 **Q. Does Dr. Won dispute the relevance of average authorized ROEs for all electric**  
12 **utilities for purposes of assessing the reasonableness of an authorized ROE for Metro**  
13 **and MO West?**

14 A. Yes. Although he compared my recommended ROE of 9.0% to the overall average of  
15 9.39% on page 26, lines 14-16 of his rebuttal testimony, he later claims the relevant  
16 benchmark is a 9.47% average authorized ROE for electric utility companies classified as  
17 vertically-integrated electric utilities.<sup>26</sup>

18 **Q. Can you provide the Regulatory Research Associates most recent quarterly report on**  
19 **major rate case decisions in order to verify any and all figures reported by each of the**  
20 **witnesses in this case?**

21 A. Yes. Attached as Schedule DM-S-4 is the most recent RRA report on major utility rate  
22 case decisions decided during 2022, as well as composite data over the last several years.

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<sup>25</sup> *Id.*, p. 27, ll. 1-3.

<sup>26</sup> *Id.*, p. 30, lines 9-11.

1 **Q. How is Dr. Won using this data to criticize your recommended authorized ROE of**  
2 **9.0% and support his recommended ROE of 9.62%?**

3 A. On pages 27 to 28 of his rebuttal testimony, Dr. Won discusses my analysis that shows that  
4 Evergy's P/E ratios have been trading at a discount to the electric utility industry average  
5 of late. My stand-alone DCF analysis of Evergy indicates that this is at least partially  
6 explained by investors perceiving Evergy's stock as being slightly riskier than average  
7 rather than due to lower growth guidance. Dr. Won believes that this information supports  
8 authorizing Metro and MO West an ROE higher than the industry average, which on page  
9 27, he indicates is 9.39%, but on page 30 he indicates it is 9.47%.

10 **Q. Do you agree that because your analysis of Evergy's stand-alone COE implies it is**  
11 **higher than the industry-average, that this justifies awarding a higher ROE?**

12 A. No. Because Evergy's stock price has been affected by uncertainty in corporate strategy  
13 (CEO turnover, changes in BOD, potential transaction noise), not business-risk uncertainty  
14 or financial risk uncertainty related to the regulated utilities, ratepayers should not be  
15 burdened with paying a higher return due to investors' concerns about these matters.  
16 Although I consider it important to analyze the parent company's COE, if its stock price is  
17 affected by factors not related to the underlying business, then this must be factored into  
18 determining a fair and reasonable ROE charged to ratepayers. As demonstrated by  
19 Missouri's passage of PISA and securitization legislation, Evergy's Missouri business-risk  
20 profile has improved, supporting a lower ROE as compared to that which was authorized  
21 in prior rate cases.

22 **Q. Dr. Won also indicates that because interest rates have increased, and "all other**  
23 **things being equal, a higher-interest rate indicates a higher required COE."<sup>27</sup> Are all**  
24 **other things equal?**

25 A. No. The economic and capital market environment post Covid-19 has been anything but  
26 typical. It is during atypical periods that utility regulatory commissions with the flexibility

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<sup>27</sup> *Id.*, p. 28, lns. 3-4.

1 to consider current market dynamics, are well-served. While higher long-term interest  
2 rates typically cause a contraction in utility stocks, this has not occurred. Recessionary  
3 fears have caused utility stocks to increase in spite of increasing interest rates. Utility  
4 stocks' defensive characteristics are currently outweighing the typical impact of the higher  
5 opportunity cost of investing in utility stocks rather than bonds.

6 **Q. Did Dr. Won request additional explanation from you regarding your analysis and**  
7 **conclusions?**

8 A. Yes. Dr. Won issued several data requests to me seeking further explanation of the  
9 rationale for my position. In my responses to Staff Data Requests No. 461, 463, and 471  
10 (*see* Schedule DM-S-5) I further explain why current market dynamics are atypical and  
11 deserve careful consideration in interpreting their impacts on the utility industry's COE  
12 and setting a fair and reasonable authorized ROE.

13 **Q. What appears to be Dr. Won's biggest concern related to your recommended ROE of**  
14 **9.0%?**

15 A. The fact that it is not formulaic. Dr. Won lists the factors he believes I considered as  
16 follows:

- 17 1) Evergy's COE (7.45% to 7.75%),
- 18 2) The electric utility industry's COE (7.0% to 7.25%),
- 19 3) Investor expectations on allowed ROEs,
- 20 4) Average electric utility authorized ROEs (9.35%), and
- 21 5) Evergy's authorized returns for its Kansas electric utility operations (9.3%).

22 **Q. Are these the only factors that you considered for purposes of your recommendation?**

23 A. No. I discussed several other factors throughout my testimony with two other primary  
24 factors being the Commission's recent awarded ROE of 9.25% for Empire and its past  
25 awarded ROEs of 9.5% for Metro in its 2014 and 2016 rate cases. Therefore, while I  
26 recognize there are many data points analyzed and described in my testimony with no

1 mathematical formula to arrive at my final ROE recommendation, I have duly considered  
2 all of the data points, providing the heaviest weight to the Commission's determination that  
3 a 9.5% authorized ROE was fair and reasonable under tighter capital market conditions  
4 around 2015, the KS Commission authorized Metro and MO Wests' affiliate a lower ROE  
5 of 9.3% in 2017, which were still tighter capital market conditions than the last few years,  
6 and the Commission authorizing Empire a 9.25% ROE when P/E ratios for utilities were  
7 at all-time highs.

8 **Q. Is it reasonable to expect a mathematical solution to an issue as subjective as**  
9 **estimating the COE and an authorized ROE informed by COE estimates?**

10 A. No. As an example, consider the wide range of COE estimates in this case. I estimate the  
11 COE to be around 7.25%, Dr. Won estimates it to be 8.18% and Ms. Bulkley estimates it  
12 to be as high 12.09%.<sup>28</sup> Therefore, three witnesses evaluating the same market data for a  
13 fairly predictable industry have almost a 5% difference in their COE estimates.  
14 Consequently, I think it is reasonable to round estimates of the COE and recommended  
15 authorized ROEs to approximate figures. For example, a COE or authorized ROE of 9.27%  
16 rather than 9.25% implies a misleading level of precision that does not exist.

17 **Q. Can you provide information that provides at least some quantified estimates for the**  
18 **changes in the electric utility industry's COE since 2015 instead of relying only on the**  
19 **P/E charts you provided in your direct and rebuttal testimonies?**

20 A. Yes. Because I still provide the results of the multi-stage DCF analysis I performed while  
21 I was with Staff, I can simply compare my current results to those from the multi-stage  
22 DCF analyses from the 2014 rate cases (*see* Schedule DM-S-6). In the 2014 Ameren  
23 Missouri rate case, the primary COE results Staff relied on for purposes of recommending  
24 the Commission authorize Ameren Missouri and Evergy Metro an ROE in the range of  
25 9.0% to 9.5%, Staff's multi-stage COE estimate was 7.65% when using the same 3%  
26 perpetual growth rate I used in the current case.<sup>29</sup> Although Staff's multi-stage COE

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<sup>28</sup> Bulkley Direct, p. 83.

<sup>29</sup> Case No. ER-2014-0258, Staff Cost of Service Report, Appendix 2, Schedule 12-1.

1 dropped to approximately 7.2% in Evergy Metro's rate case just four months later, Staff  
2 continued to recommend a 9.0% to 9.5% ROE for Evergy Metro. In this current rate case,  
3 when I performed a multi-stage DCF analysis using the same approach as Staff in the 2014  
4 rate case, the multi-stage COE estimate is approximately 6.8%. Consequently, a properly  
5 performed COE analysis with reasonable inputs corroborates my conclusion in my direct  
6 testimony, which is that the utility industry's cost of equity is lower than at the time the  
7 Commission first determined a 9.5% authorized ROE was reasonable for its electric  
8 utilities. These macro conditions, coupled with the fact that Missouri's electric utilities are  
9 now afforded the opportunity to take advantage of investor-friendly ratemaking  
10 mechanisms due to legislative changes, do not support raising Metro's and MO West's  
11 authorized ROEs above 9.5%. If anything, current capital market conditions support an  
12 authorized ROE of no higher than 9.25%.

13 **Q. Did you analyze the same companies in the current rate case as Staff did in the 2014**  
14 **rate cases?**

15 A. Yes with the exception that Great Plains Energy, Westar Energy, and TECO Energy no  
16 longer exist as separately publicly-traded companies. Additionally, beginning in 2019 I  
17 began to select a broad group of companies with electric utility operations, which are  
18 members of the Edison Electric Institute. However, the companies I analyzed in 2014 are  
19 a subset of my current proxy group.

20 **Q. If you limited your comparison to the same companies you analyzed in 2014, what is**  
21 **the approximate implied COE changes since 2014?**

22 A. The COE for the same electric utilities has declined by approximately 70 basis points since  
23 the 2014 UE rate case and 20 basis points since the 2014 Metro rate case.

24 **Q. Are there any companies that should be excluded from this comparison due to**  
25 **fundamental changes in their business risk profiles between these periods?**

26 A. Yes. Ameren had been exiting riskier energy merchant operations at the time of the 2014  
27 rate case, which caused its COE to be influenced by this uncertainty. Additionally, over

1 the past several years, DTE and OGE have had significant exposure to commodity price  
2 risk through their midstream operations.

3 **Q. After excluding these companies, how much has the COE changed since 2014?**

4 A. It has declined approximately 50 basis points based on Staff's multi-stage DCF analysis in  
5 UE's 2014 electric rate case and 10 basis points since Metro's 2014 rate case a few months  
6 later.

7 **Q. Dr. Won disagrees with your recommended ratemaking common equity ratios of 48%**  
8 **for both Metro and MO West. He claims that subsidiary capital structures are more**  
9 **appropriate. Did Dr. Won recommend the use of Metro's and MO West's capital**  
10 **structures for ratemaking in this case?**

11 A. Sort of. Dr. Won's recommended ratemaking capital structures is based on MO West's  
12 and Metro's DR response which indicates that Evergy targets a 50% common equity ratio  
13 for itself, Metro, and MO West.<sup>30</sup> Dr. Won also indicates that the average actual capital  
14 structures for 2020 and 2021 support the companies' DR responses.<sup>31</sup> Therefore he  
15 considers this as an appropriate ratemaking common equity ratio.

16 **Q. Does Dr. Won compare Evergy's capital structure to Metro's and MO West's for**  
17 **purposes of concluding that a 50% common equity ratio is reasonable for**  
18 **ratemaking?**

19 A. Yes. Table 1 on page 22 of Dr. Won's direct testimony shows his comparison of each  
20 company's capital structures. His table indicates that each company's averaged common  
21 equity ratios for the period 2020 through 2021 were in the 49% range. He indicates that  
22 because each company's actual and targeted common equity ratios approximate 50%, this  
23 is a reasonable common equity ratio.

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<sup>30</sup> Won Direct, p. 22, lns. 4

<sup>31</sup> *Id.*, p. 22, l. 17 – p. 23, l. 9.

1 **Q. What does Dr. Won indicate as Evergy's average common equity ratio for 2020 and**  
2 **2021?**

3 A. 49.21%.

4 **Q. Why does Dr. Won conclude that Evergy has a higher common equity ratio than you**  
5 **determined in your direct testimony?**

6 A. Different sources, different data included in long-term debt, and different averaging  
7 methodologies.

8 **Q. What source did Dr. Won rely on for his capital balances?**

9 A. Evergy's response to Staff Data Request No. 115. According to Dr. Won's workpapers, it  
10 appears he compared the figures to Evergy's SEC Form 10-K filings, but not all figures  
11 reconcile.

12 **Q. What is the main difference between your reported long-term debt balance and his**  
13 **reported long-term debt balance?**

14 A. I included current maturities on long-term debt, but he excluded the current maturities. I  
15 included leases in the long-term debt balance, but he excluded them.

16 **Q. Did you intend to include leases in the long-term debt balance?**

17 A. No. I had used an S&P Global Market Intelligence balance sheet template that reported  
18 leases as long-term debt. I have now removed such from the long-term debt balance.

19 **Q. Should current maturities of long-term debt be included in the capital structure as**  
20 **long-term debt?**

21 A. Yes. The cost of the maturing long-term debt is included in the embedded cost of long-  
22 term debt. Although for accounting purposes maturing long-term debt is identified as a  
23 short-term liability, it is fairly standard and typical for such maturing long-term debt to be



1 refinanced with new long-term debt, remaining a constant component of the capital  
2 structure.

3 **Q. After analyzing Evergy's, Metro's and MO West's capital structure information**  
4 **through June 30, 2022, does your analysis still show that Evergy maintains more**  
5 **leverage than its regulated utility subsidiaries?**

6 A. Yes. Including short-term debt in Evergy's capital structure shows an even larger  
7 discrepancy between Evergy's common equity ratio compared to Metro and MO West.  
8 During the first quarter of 2022, Evergy made a \$200 million equity infusion into MO West  
9 from a \$500 million 1-year term loan it issued in February 2022.<sup>32</sup> Based on Evergy's June  
10 30, 2022, balance sheet, Evergy's common equity ratio is now less than 44% of its total  
11 capital structure (including short-term debt). If I ignored Evergy's \$2.375 billion of short-  
12 term debt, then this would imply that Evergy had a common equity ratio of 49.38% at June  
13 30, 2022.

14 **Q. Dr. Won cites to four factors that may be considered for purposes of evaluating the**  
15 **independence of subsidiary's capital structures versus that of its parent company.**  
16 **Are these factors definitive as it relates to a potential binary decision of choosing a**  
17 **subsidiary versus a parent company capital structure?**

18 A. No. While each of these factors can be considered independently, it is also important to  
19 consider the interplay of each of these factors and the underlying rationale for each of the  
20 factors. For example, it is important to understand the rationale for parent guarantees and  
21 whether diversification into non-utility operations causes the consolidated parent company  
22 capital structure to be more or less comparable regarding the regulated utility subsidiaries'  
23 debt capacity.

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<sup>32</sup> Evergy SEC Form 10-Q, March 31, 2022, p 36 (Note 6 of the Notes to Financial Statements) and Evergy Missouri West, Inc.'s Unaudited Consolidated Financial Statements, March 31, 2022, p. 18 (Note 9 of the Notes to Financial Statements).

1 **Q. Is Dr. Won correct that Metro and MO West issue their own debt?**

2 A. Yes. Each subsidiary issues its own long-term debt and even commercial paper to third-  
3 party debt markets. However, as is evident from significant increases in money pool  
4 transactions between Metro and MO West, as well as a significant amount of holding  
5 company short-term borrowings, the lines are not as clearly defined as implied by  
6 recognizing that each subsidiary issues its own debt.

7 Evergy's issuance of commercial paper is causing the lines to be blurred as to the third  
8 guideline as well. Although it is clear that Evergy already in fact had double leverage, *i.e.*  
9 long-term debt outstanding at the holding company and subsidiary level, the long-term debt  
10 had been issued to buy back common stock. While this leverage was not used to purchase  
11 common equity in the subsidiary, its use has the same impact on the consolidated  
12 company's financial risk. However, in February 2022, Evergy raised \$500 million through  
13 a 1-year term loan, of which \$200 million was used to fund a common equity infusion into  
14 MO West. Under affiliate transaction rules, MO West should only be charged for the cost  
15 of the capital used to make such an equity infusion. The weighted-average interest rate on  
16 Evergy's term loan was 1.13% at March 30, 2022 and 2.33% at June 30, 2022, significantly  
17 below the 11.31% pre-tax ROE Evergy is requesting it be allowed in revenue requirement  
18 for this capital infusion. This is an example of a lack of significant financing separation as  
19 it relates the third guideline.

20 The second guideline also needs to be considered carefully as to the interpretation of the  
21 need for a parental guarantee and the interaction of this guideline with the fourth guideline,  
22 whether a consolidated enterprise is diversified in non-utility operations. A holding  
23 company that only owns regulated utility subsidiaries (considered a pure-play regulated  
24 utility) derives its creditworthiness from the low-risk profile of its regulated utility  
25 subsidiaries. In fact, when selecting comparable companies to estimate the COE for  
26 Metro's and MO West's 100% vertically-integrated electric utilities, the goal is to select  
27 publicly-traded holding companies that are mostly confined to regulated utility operations.  
28 The COE for these holding companies should then be a function of the low business risk

1 associated with the regulated subsidiaries AND the financial risk (*i.e.* use of debt in the  
2 capital structure) contained in the consolidated capital structure.

3 **Q. Does Ms. Bulkley’s discussion of the fourth guideline illustrate Dr. Won’s**  
4 **misinterpretation of the logic for this guideline?**

5 A. Yes. Ms. Bulkley attempts to discredit the relevance of Evergy’s consolidated capital  
6 structure by emphasizing that Evergy *is* diversified by having a minor investment interest  
7 in Transource Energy, LLC, which is involved in the development of competitive electric  
8 transmission projects, among other non-regulated activities.<sup>33</sup> This is in stark contrast to  
9 Dr. Won’s emphasis that “in 2020, Evergy Inc.’s non-utility assets and revenue are less  
10 than 1.0% of Evergy Inc.’s total assets and total revenue. This not concerning because  
11 Evergy Inc.’s non-utility operations are **insignificant**” (emphasis added).<sup>34</sup>

12 If a holding company’s operations are largely confined to regulated utilities, then the  
13 proportion of debt maintained at the consolidated level provides the most objective and  
14 transparent view as to managements’ opinion of an economic, yet stable proportion of  
15 leverage the low business-risk profile of its utility assets can sustain. If a holding company  
16 also had significant non-regulated operations, then one would expect the holding company  
17 to balance the higher business risk of the non-regulated operations by targeting a less  
18 leveraged capital structure than its regulated utilities could support.

19 Evergy is predominantly a pure-play regulated vertically-integrated electric utility. Its  
20 consolidated capital structure strategy is consistent with its low-risk regulated utility  
21 subsidiaries.

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<sup>33</sup> Bulkley Rebuttal, p. 16, lns. 10-13.

<sup>34</sup> Won Rebuttal, p. 35, lns. 1-4.

1 **SUMMARY AND CONCLUSIONS**

2 **Q. Can you summarize your main conclusions related to your surrebuttal testimony in**  
3 **this case?**

4 A. Yes. As it relates to capital structure, the other parties have not performed a deep and  
5 thorough analysis of the interrelationship of Evergy, Metro and MO West's capital flows.  
6 In fact, Evergy's increasing use of holding company short-term debt to either directly fund  
7 equity infusions or indirectly fund dividends to shareholders rather than relying on  
8 distributions from its subsidiaries allows for not only manipulation of subsidiary capital  
9 structures for purposes of targeting a common equity ratio for ratemaking, but as is  
10 demonstrated by MO West's significant per books short-term debt (both third party and  
11 affiliate) and Metro's insignificant per books short-term debt, these transactions cause  
12 distortions in capitalization rates assigned to each company. The most direct means to  
13 protect against these affiliate financing transaction abuses is to look to the ultimate parent  
14 company's capitalization targets and policies for guidance for a fair and reasonable costs  
15 of capital. This is the basis for my positions in these cases.

16 As it relates to an authorized ROE, the Commission should simply be aware of Evergy's  
17 own actions, which is its allocation of significant amounts of capital to its Missouri  
18 jurisdiction, of which 88% is PISA eligible. If a 9.5% authorized ROE was considered  
19 reasonable over seven years ago when macro capital market conditions were tighter and  
20 Missouri did not have the current suite of favorable utility ratemaking and cost recovery  
21 mechanisms (i.e. securitization), then this ROE is no longer reasonable because of reduced  
22 capital costs and lower business risks. Consequently, I continue to recommend an  
23 authorized ROE of 9%.

24 **Q. Does this conclude your testimony?**

25 A. Yes.

**BEFORE THE PUBLIC SERVICE COMMISSION  
OF THE STATE OF MISSOURI**

In the Matter of Evergy Metro, Inc.                    )  
d/b/a Evergy Missouri Metro's Request            )  
for Authority to Implement a General                )  
Rate Increase for Electric Service                )  
In the Matter of Evergy Missouri West,            )  
Inc. d/b/a Evergy Missouri West's                 )  
Request for Authority to Implement a                )  
General Rate Increase for Electric                )  
Service    )

Case No. ER-2022-0129

Case No. ER-2022-0130

**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 and true-up direct 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  
Utility Regulatory Manager

Subscribed and sworn to me this 16<sup>th</sup> day of August 2022.



TIFFANY HILDEBRAND  
My Commission Expires  
August 8, 2023  
Cole County  
Commission #15637121

  
Tiffany Hildebrand  
Notary Public

My Commission expires August 8, 2023.