

Exhibit No. 407

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Sponsoring Party: Public Counsel
Case No.: ER-2021-0240

SURREBUTTAL TESTIMONY

OF

DAVID MURRAY

Submitted on Behalf of the Office of the Public Counsel

**UNION ELECTRIC COMPANY
D/B/A AMEREN MISSOURI**

FILE NO. ER-2021-0240

**

**

**Denotes Confidential Information
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November 5, 2021

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UNION ELECTRIC COMPANY d/b/a AMEREN MISSOURI

FILE NO. ER-2021-0240

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**
5 **in this case?**

6 A. Yes.

7 **Q. What is the purpose of your testimony?**

8 A. To respond to Company witnesses' Darryl T. Sagel's and Ann E. Bulkley's rebuttal
9 testimonies as it relates to rate of return ("ROR") and capital structure. I will also address
10 the rebuttal testimony of Staff witness Peter Chari.

11 **Q. What are some important practical issues that you raised in your Direct Testimony**
12 **that the Company did not address in their rebuttal testimony?**

13 A. The Company ignored the following issues I raised in my Direct Testimony:

- 14 1. The fact that Ameren Illinois' and Ameren Missouri's cost of capital is
15 very similar, which is easily determined by observing current yields on
16 Ameren Missouri bonds and Ameren Illinois bonds. Based on latest
17 bond yields on 30-year bonds issued by both Ameren Illinois and
18 Ameren Missouri, the cost of capital is essentially the same for both
19 companies; and
20 2. Considering the cost of capital for Ameren Missouri and Ameren Illinois
21 is essentially the same, the fact that a higher allowed ROR for

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1 investments in Ameren Missouri's integrated electric utility operations
2 ("electric utility) will create more shareholder wealth than an investment
3 in Ameren Illinois' electric transmission and distribution utility.

4 **Q. In what order do you plan to address the issues raised in each of the witnesses'**
5 **testimonies?**

6 A. I will address capital structure first, which was the sole ROR issue addressed by Mr. Sagel.
7 Ms. Bulkley also discusses Ameren Missouri's proposed capital structure as it relates to
8 other capital structures within the industry. Mr. Chari also disagrees with the premise of
9 using Ameren Corp as a proxy for a fair and reasonable ratemaking capital structure for
10 Ameren Missouri.

11 I will then address Ms. Bulkley's and Mr. Chari's responses to my recommended allowed
12 ROE of 9.0% for Ameren Missouri's integrated electric utility operations ("electric
13 utility").

14 **Q. Can you summarize the main points related to your disagreement with the other**
15 **witnesses about an appropriate ratemaking capital structure to set Ameren**
16 **Missouri's ROR in this case?**

17 A. Yes. The other witnesses support the use of Ameren Missouri's per books capital
18 structure. They maintain this is the appropriate ratemaking capital structure because, in
19 their view, it is independently managed for its own benefit, and presumably for the benefit
20 of Ameren Missouri's ratepayers. While I agree that Ameren Missouri's capital structure
21 is carefully managed, it is managed for one primary purpose, achieving a constant 52%
22 authorized equity ratio regardless of changes in business and economic conditions. This
23 has become quite apparent since 2018. Even in light of Ameren Missouri's reduced
24 business risk due to more favorable ratemaking mechanisms such as plant in service
25 accounting ("PISA") and very favorable (i.e. low) debt costs, Ameren Missouri's equity
26 ratio hasn't budged from the 52% target over the last ten years. Ratepayers footing the bill
27 for a 52% equity ratio would be less egregious if Ameren Corp targeted this more

1 conservative level for itself, but instead, it has become more aggressive in issuing debt
2 since 2018.

3 My response to the other witnesses' capital structure arguments will show that Ameren
4 Missouri's capital structure has not been managed for its own best interests and for the best
5 interests of its ratepayers. Ameren Missouri's ratepayers are paying for the costs of more
6 shareholder friendly ratemaking mechanisms, but not receiving the benefit of the lower-
7 cost capital structure they support (i.e. higher debt capacity).

8 **DARRYL T. SAGEL'S REBUTTAL TESTIMONY**

9 **Q. Does Mr. Sagel admit that since Ameren Missouri was allowed to PISA subsequent**
10 **to the passage of Senate Bill ("SB") 564, Ameren Corp's debt capacity has increased?**

11 A. Yes, but it is his position that this is only one factor Moody's considered in lowering
12 Ameren Corp's funds from operations to debt ("FFO/debt")¹ downgrade threshold to 17%
13 from 19%. Mr. Sagel indicates Ameren Corp's increased debt capacity was also due to "a
14 strong track record of strategy execution within the supportive regulatory frameworks of
15 Ameren Corporation's subsidiaries, Ameren Illinois and ATXI."²

16 **Q. Did Moody's lower its FFO/debt downgrade threshold for its other operating**
17 **subsidiaries, Ameren Illinois or ATXI?**

18 A. Not that I am aware.

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

21 A. No.

¹ Although there are subtle differences between Moody's 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.

² Sagel Rebuttal, p. 29, lns. 4-6.

1 **Q. Then why would Moody's lower Ameren Corp's downgrade threshold rather than**
2 **for each of the "independent" subsidiaries?**

3 A. Because the officers who are representing Ameren Corp, Ameren Missouri, Ameren
4 Illinois and ATXI when interacting with the rating agencies are acting as a fiduciary for
5 Ameren Corp rather than each of its subsidiaries, including Ameren Missouri.

6 **Q. Mr. Sagel indicates that Moody's rejected Ameren Corp's management's argument**
7 **to **** _____
8 _____

9 ****³ Is Mr. Sagel's recollection of these events accurate?**

10 A. No. ** _____
11 _____
12 _____
13 _____
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16 _____
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20 **

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

23 A. Yes. Since 2019, Ameren Corp has doubled the percentage of holding company debt it
24 uses to finance its subsidiaries.

³ *Id.*, p. 21, lns. 6-10.

1 **Q. Has Ameren Corp shared this lower cost of capital with Ameren Missouri's**
2 **ratepayers by lowering the equity ratio it requests the Commission apply its**
3 **authorized ROE?**

4 A. No.

5 **Q. Are you aware of other companies the Commission should consider when evaluating**
6 **Ameren Corp's arguments that Ameren Missouri's assets cannot support more debt**
7 **and lower FFO/debt ratios?**

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

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

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

12 **Q. What have Evergy Metro's FFO/debt ratios been the last three years?**

13 A. 18.8% in 2020, 17.8% in 2019, and 18.7% in 2018.⁴

14 **Q. Has Evergy Metro been placed on a "negative watch" or even a more general**
15 **"negative outlook" because its FFO/debt ratios have been below the 19% threshold**
16 **Mr. Sagel claims Ameren Missouri is required to maintain to avoid being downgraded**
17 **by Moody's?**

18 A. No. Evergy Metro currently has a "stable outlook" despite its FFO/debt ratio being below
19 19% for the last three years. Moody's indicates that it expects Evergy Metro's FFO/debt
20 ratios to be in the "high teens" for the next 12-18 months. Moody's indicates it may
21 consider a downgrade if Evergy Metro's FFO/debt falls below 18% on a sustained basis.

⁴ Moody's Credit Opinion, Evergy Metro Inc., April 29, 2021, Exhibit 2, p. 3.

1 **Q. Are you aware of any compelling reasons why Moody's should view Evergy Metro's**
2 **financial risk thresholds differently than Ameren Missouri's?**

3 A. No.

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

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

9 **Q. Was Evergy Metro placed on a "negative watch" or "negative outlook" after the**
10 **Commission Order?**

11 A. No.

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

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

15 **Q. Mr. Sagel warns of potential negative credit and cost of capital ramifications if the**
16 **Commission were to authorize Ameren Missouri a lower common equity ratio than**
17 **that shown on Ameren Missouri's books.⁵ Did Ameren Corp use the same strategy**
18 **when disputing a lower authorized common equity ratio for its subsidiary, Ameren**
19 **Illinois?**

20 A. Yes. Ameren Corp used the same strategy. In testimonies filed in Ameren Illinois rate
21 cases, Ameren Illinois witnesses recommended and vigorously defended the use of Ameren
22 Illinois' actual capital structure, which contained a common equity ratio as high as
23 54.279% in Docket No. 12-0001.⁶ The arguments in the Ameren Illinois rate cases were

⁵ Sagel Rebuttal, p. 23, ll. 1-14.

⁶ Illinois Docket No. 12-0001, Schedule D-1 Sponsored by Ryan J. Martin

1 quite similar to those in this case. Ameren Illinois' witnesses indicated Ameren Illinois
2 had to maintain a higher common equity ratio in order to offset higher business risks
3 associated with the Illinois regulatory environment.⁷

4 **Q. What equity ratio did the Illinois Commerce Commission (ICC) Staff witness**
5 **recommend in that case?**

6 A. 51.49%.

7 **Q. What did the ICC authorize?**

8 A. 51.49%

9 **Q. What common equity ratio did Ameren Illinois recommend in Docket No. 13-0301?**

10 A. 54.62%.

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

12 A. 51%.

13 **Q. What was the premise for ICC Staff's recommended common equity ratio?**

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

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

16 A. 51%.

17 **Q. What common equity ratio did Ameren Illinois recommend in Docket No. 14-0317?**

18 A. 51%.

⁷ Illinois Docket No. 12-001, Ryan J. Martin Rebuttal Testimony, p. 5, l. 97 through p. 6, l. 116.

1 **Q. What about the ICC Staff?**

2 A. 51%.

3 **Q. Why did they recommend the same common equity ratio?**

4 A. Because the ICC Staff and Ameren Illinois agreed to use a 51% common equity ratio for
5 purposes of that case.

6 **Q. Did they agree to use this equity ratio in subsequent cases?**

7 A. No. They agreed to use a 50% common equity ratio, which was later codified into law.

8 **Q. Over the period of all of these cases in which Ameren Illinois' fair and reasonable**
9 **ratemaking capital structure was debated and decided by the ICC, were Ameren**
10 **Illinois' credit ratings put on a negative outlook or watch?**

11 A. No.

12 **Q. Are you surprised management only lobbied to have Ameren Corp's credit metrics**
13 **relaxed, but not Ameren Missouri's?**

14 A. No.

15 **Q. Why?**

16 A. Because Ameren Corp's and Ameren Missouri's officers and directors often serve in
17 multiple and revolving functions/positions within the Ameren Corp family of companies.

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

19 A. He is the Vice President and Treasurer.

20 **Q. Does Mr. Sagel hold this same position with Ameren Corp and its subsidiaries?**

21 A. Yes. Mr. Sagel is Vice President and Treasurer for Ameren Corp, Ameren Illinois and
22 Ameren Transmission Company of Illinois (ATXI).

1 **Q. Do you have concerns about Mr. Sagel’s lack of bargaining for Ameren Missouri’s**
2 **financial interest?**

3 A. Yes. The fact that Mr. Sagel seems to simply accept that Ameren Missouri has not received
4 any credit for its reduced business risk profile is disturbing. It certainly illustrates to the
5 extent Ameren Missouri does have its own board of directors (“BOD”) and officers, they
6 clearly are not looking out for Ameren Missouri’s financial interest and the interest of its
7 customers. If Ameren Missouri’s interest, and that of its ratepayers, were being protected,
8 then Ameren Missouri’s officers would have bargained for Ameren Missouri’s rightful
9 debt capacity. As I will demonstrate later, this is even more concerning considering the
10 fact that Ameren Missouri’s cash flows have supported Ameren Corp’s ability to finance
11 its investments in its other subsidiaries as well as paying dividends to Ameren Corp’s
12 shareholders over the last several years.

13 **Q. What evidence do you have that Ameren Missouri’s officers have not bargained for**
14 **its own independent interests?**

15 A. Ameren Corp’s December 17, 2018 presentation to Moody’s (Schedule DM-S-1) clearly
16 shows that ** _____
17 _____
18 _____
19 _____
20 _____ **

21 **Q. How do you know Ameren Missouri’s reduced business risk resulted in a lower**
22 **FFO/debt threshold for Ameren Corp?**

23 A. Because Ameren’s management made this argument to Moody’s in order to convince them
24 that Ameren’s FFO/debt threshold should be reduced. Ameren indicated the following
25 during the Ameren Corp Finance Committee Meeting on February 7, 2019:

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Ameren also indicated the following during it Financing Committee Meeting on May 2, 2019:

** _____

_____ ***

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

A. I found no evidence of Ameren Corp performing an analysis on Ameren Missouri's behalf, or Ameren Missouri performing this analysis on its own behalf, to compare Ameren Missouri's FFO/debt metrics to that of its peers in order to attempt to persuade Moody's to reduce Ameren Missouri's FFO/debt threshold.

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

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

Q. Were these individuals 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.

⁸ Ameren Corp's Finance Committee Meeting, February 7, 2019, p. 24.
⁹ Ameren Corp's Finance Committee Meeting, May 2, 2019, p. 87

1 **Q. Did they serve in the same capacity for Ameren Missouri and Ameren Illinois at the**
2 **time?**

3 A. Yes.

4 **Q. Are these individuals employed by Ameren Corp?**

5 A. No. Ameren Services Corporation employs each of these individuals.

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

8 A. No.

9 **Q. What do you conclude based on this information?**

10 A. The only way to ensure Ameren Missouri's ratepayers are given their due consideration
11 for providing the Company more certain cost recovery from PISA, which allows for higher
12 debt capacity, is to adjust Ameren Missouri's common equity ratio to be consistent with
13 that of Ameren Corp's on a consolidated basis. This is the level at which Ameren Corp is
14 balancing its business risk and financial risk to achieve a lower cost of capital and still
15 maintain a reasonably stable investment grade credit rating. Adopting a capital structure
16 consistent with Ameren Corp's consolidated capital structure ensures Ameren Missouri's
17 ratepayers receive the benefit of the additional debt capacity made possible by SB 564.
18 Although Mr. Sagel acknowledges that SB 564 was at least the tipping point for Ameren
19 Corp being allowed a more leveraged profile, he stands firm in not giving any consideration
20 to Ameren Missouri's customers in the form of a more leveraged and cost efficient capital
21 structure. In my opinion, this is one of the clearest examples of the need for the
22 Commission to assert its authority to ensure a fair and reasonable outcome for ratepayers.
23 Otherwise, Ameren Corp's shareholders are unfairly enriched through the use of Ameren
24 Missouri's ratepayer supported debt capacity.

1 **Q. Are there other reasons as to why the Companies' officers haven't bargained to have**
2 **Ameren Missouri's FFO/debt thresholds reduced?**

3 A. Yes. Ameren Missouri's FFO/debt ratios have typically been more consistent with that of
4 an 'A' rated credit rather than a 'Baa' credit.¹⁰

5 **Q. What Stand-Alone Credit Profile ("SACP") did S&P assign to Ameren Missouri in**
6 **past?**

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

9 **Q. What was the primary cause for S&P assigning Ameren Missouri a stronger SACP?**

10 A. Because of Ameren Missouri's healthier financial risk profile, e.g. higher FFO/debt ratios.
11 However, because Ameren Corp did not have as strong of a financial risk profile ("FRP"),
12 Ameren Missouri's S&P credit rating was limited to a 'BBB+'.

13 **Q. Did Ameren Missouri's stronger FRP provide credit support to Ameren Corp while**
14 **it financially supported ATXI and AIC?**

15 A. Yes. During the period in which Ameren was supporting investment in ATXI and AIC,
16 Ameren Missouri's FFO/debt ratios were around 24% or higher, which was significantly
17 above the 19% FFO/debt threshold required to maintain a 'Baa1' credit rating. Ameren
18 Missouri could have issued more debt during this period and still had a comfortable
19 FFO/debt margin above 19%. However, if Ameren Missouri had done so, it would have
20 caused Ameren Corp's consolidated FFO/debt ratio to be lower. Maintaining a higher
21 FFO/debt ratio at Ameren Corp over this period was important for Ameren Corp because
22 it was regularly accessing the capital markets, such as to issue commercial paper, in order
23 to fund investment in ATXI, which required significant amounts of capital. After
24 accumulating a significant amount of short-term debt at Ameren due to its investment in
25 ATXI and its refinancing of a \$425 million long-term bond, Ameren Corp issued \$700

¹⁰ Moody's Credit Opinion, Union Electric Company, September 13, 2021, p. 8.

1 million of bonds in 2015, which was a year in which Ameren Missouri had a FFO/debt
2 ratio of 26.7%¹¹. This compared to Ameren Corp's consolidated FFO/debt ratio of 24.4%
3 during the same year.¹²

4 **Q. Staff witness Mr. Chari claims that if Ameren Missouri's capital structure was**
5 **managed to a 45% common equity ratio, it may impair Ameren Missouri's credit**
6 **ratings because it would increase Ameren Missouri's FRP.¹³ Does Mr. Chari provide**
7 **support for his view?**

8 A. Not really. Mr. Chari indicates that if Ameren Missouri's capital structure were managed
9 to a 45% common equity ratio this "might mean that Ameren Missouri's FRP would
10 worsen and jeopardize its current credit ratings, and subsequently lead to an increase in its
11 cost of capital."¹⁴

12 **Q. What FRP does S&P assign to Ameren Corp at the 45% equity ratio it targets for its**
13 **own consolidated capital structure?**

14 A. 'Significant.'¹⁵

15 **Q. What FFO/debt ratios does S&P project over the next three years for Ameren Corp**
16 **on a consolidated basis?**

17 A. 15% to 17%.¹⁶

18 **Q. What FFO/debt ratio does S&P project over the next three years for Ameren**
19 **Missouri?**

20 A. 18% to 22%.¹⁷

¹¹ Moody's Credit Opinion, Union Electric Company, March 29, 2019, Exhibit 2, p. 2.

¹² Moody's Credit Opinion, Ameren Corporation, March 29, 2019, Exhibit 2, p. 2.

¹³ Chari Rebuttal, p. 20, l. 18 – p. 21, l. 2.

¹⁴ *Id.*, p. 20, lns. 19-21.

¹⁵ S&P Global – RatingsDirect, Ameren Corp, April 27, 2021, p. 14.

¹⁶ *Id.*, p. 6.

¹⁷ S&P Global – RatingsDirect, Union Electric d/b/a Ameren Missouri, April 27, 2021, p. 5.

1 **Q. If Ameren Missouri had a higher percentage of debt in its capital structure, would**
2 **this cause Ameren Corp's consolidated financial risk to increase to a level that may**
3 **cause a downgrade to Ameren Corp's credit rating?**

4 A. Yes. However, it is fully within Ameren Corp's control to reduce the amount and
5 percentage of holding company debt to fairly share the debt capacity supported by Ameren
6 Missouri's ratepayers through more favorable ratemaking mechanisms, which provide
7 more certain recovery and reduced regulatory lag. If Ameren Corp reduces the holding
8 company debt by the same amount of the increase in Ameren Missouri's' debt, Ameren
9 Corp's consolidated capital structure would not change.

10 **Q. Did Mr. Sagel provide a quantification of the potential impact the Commission's**
11 **adoption of your capital structure recommendation would have on Ameren**
12 **Missouri's FFO/debt ratios?**

13 A. Yes. Mr. Sagel estimates that if Ameren Missouri's revenue requirement in 2020 had been
14 premised on my recommended capital structure containing a 45% common equity ratio,
15 this would have reduced Moody's FFO/debt ratio to 15.2% from 18.9%.¹⁸

16 **Q. Do you dispute Mr. Sagel's estimate of the pro forma impact your recommended**
17 **ROR would have on Ameren Missouri's 2020 FFO/debt ratio?**

18 A. No. Assuming the same ROE (9.5%) is applied to Mr. Sagel's recommended capital
19 structure compared to my recommended capital structure, this causes a \$49.3 million
20 difference in revenue requirement for both Ameren Missouri's gas and electric rate cases.
21 Assuming Ameren Missouri then issues an additional \$768.2 million in long-term debt to
22 target a 45% common equity ratio, then this would create additional after-tax interest
23 expense of approximately \$21.2 million if this debt has the same embedded cost as Ameren
24 Missouri's current debt outstanding (3.85%). However, as I explained in my direct
25 testimony,¹⁹ the likely cost of new debt for Ameren Missouri would closer to 2.88%. But

¹⁸ Sagel Rebuttal, p. 36, l. 1 – p. 37, l. 8.

¹⁹ Murray Direct, p. 41, ll. 1-9.

1 this lower interest expense would only cause Mr. Sagel's FFO/debt ratio to increase by
2 1/10th of a percent (15.3% vs. 15.2%).

3 **Q. What was Ameren Missouri's FFO/debt ratio for the last twelve months through June**
4 **30, 2021?**

5 A. 14.8%.²⁰

6 **Q. Did Moody's downgrade Ameren Missouri or put it on a negative outlook as a result**
7 **of this lower FFO/debt ratio?**

8 A. No. Moody's indicated because Ameren Missouri's lower FFO was due to higher fuel
9 costs and power purchases that are recoverable through the fuel adjustment clause (FAC)
10 and the purchased gas adjustment (PGA) regulatory rate recovery mechanisms (i.e. lower
11 business risk), it was not concerned about the long-term expectations of an FFO/debt in the
12 low 20% range.²¹

13 **Q. If the Commission set Ameren Missouri's ROR based on your recommended capital**
14 **structure, what impact would the approximate 3.5% to 4.0% reduction to Ameren**
15 **Missouri's FFO/debt ratio have on Ameren Missouri's projected FFO/debt ratios?**

16 A. They would be in the 18.5% to 19.5% range over the next several years, which is above
17 the lower threshold of 17% Moody's set for Ameren Corp. to maintain its 'Baa1' rating.

18 **Q. Would this not cause Ameren Corp's FFO/debt ratios to fall below 17%?**

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

²⁰ Moody's Credit Opinion, September 13, 2021, p. 6.

²¹ *Id.*

1 **Q. Has Ameren Corp's other financial interests impaired Ameren Missouri's financing**
2 **flexibility in the past?**

3 A. Yes. There is no doubt that Ameren Corp's financing and business risks have impacted
4 Ameren Missouri's financing flexibility in the past. Ameren Missouri's was foreclosed
5 access to commercial paper markets in August 2008 due to its Moody's short-term credit
6 rating being downgraded to P-3. Ameren Missouri's short-term rating was downgraded
7 due to Moody's downgrading Ameren Corp' long-term rating to 'Baa3'. This downgrade
8 was primarily caused by financial difficulties at Ameren Missouri's affiliates. Because
9 S&P already rated Ameren Corp at a 'BBB-', which meant Ameren Missouri was also
10 rated 'BBB-', Ameren Missouri had an A-3 short-term rating. These Tier-3 short-term
11 ratings foreclosed Ameren Missouri's access to short-term credit markets, which proved to
12 be quite costly to Ameren Missouri ratepayers because of liquidity concerns. Ameren
13 Missouri ratepayers were charged for carrying costs due to the delay in construction at
14 Ameren Missouri's Sioux Scrubber plants.

15 **Q. How do you know these downgrades foreclosed Ameren Missouri's ability to access**
16 **commercial paper?**

17 A. Because Kansas City Power & Light Company had at least one Tier-2 rating, it was able
18 to continue to issue commercial paper to fund its power plant construction at the time.

19 **Q. Are you attempting to reopen an issue that was resolved in Case No. ER-2011-0028?**

20 A. No. I am simply providing this testimony to illustrate the hypocrisy of Mr. Sagel's
21 expressed concerns about Ameren Missouri's ratepayers paying a higher ROR to provide
22 financial stability for a parent company that hasn't always reciprocated. If Ameren Corp
23 wants Ameren Missouri's equity ratio to be set around 52%, then Ameren Corp should
24 issue more equity and less debt in order achieve an equity ratio more consistent with the
25 52% it apparently considers important to maintain financial flexibility.

1 **Q. Mr. Sagel indicates that you have not provided sufficient proof that Ameren**
2 **Missouri’s cost of debt has declined due to the passage of SB 564.²² Did Mr. Sagel**
3 **correctly interpret your testimony with this statement?**

4 **A.** No. My argument is that Ameren Missouri’s regulated utility assets can support a greater
5 portion of debt in its capital structure than it has in the past. Ameren Missouri’s lower
6 business risk creates additional debt capacity while still being able to maintain the same
7 credit rating. I argue that the reduced business risk ultimately supported by ratepayers
8 allows for a lower cost of capital due to higher debt capacity. This benefit should be shared
9 with ratepayers in the form of a more leveraged ratemaking capital structure. Being that
10 debt has a much lower cost than equity, this would result in a lower cost of capital charged
11 to Ameren Missouri ratepayers. It is not fair to keep Ameren Missouri’s equity ratio
12 constant over time when there have been fundamental changes to Ameren Missouri’s
13 ability to recover investments through the PISA tracker and RESRAM rider. This
14 unfairness is magnified due to the fact that Ameren Corp is using this reduced business risk
15 to support the issuance of more holding company debt to leverage shareholder returns.

16 **Q. Mr. Sagel discusses Moody’s concerns about the strain the Tax Cut and Jobs Act**
17 **(“TCJA”) could have on the utility industry’s credit metrics such as the FFO/debt**
18 **ratio. He indicates that the Commission can help support Ameren Missouri’s ability**
19 **to retain its current credit ratings by authorizing its requested higher equity ratio of**
20 **51.93%.²³ How do you respond to Mr. Sagel’s plea?**

21 **A.** It is offensive. First, it is noteworthy that it has been 3-4 years since the TCJA was passed
22 and dealt with in regulatory proceedings with the Commission. Second, it is hypocritical
23 to request Ameren Missouri’s ratepayers to pay a higher amount of net income on a more
24 conservative 52% common equity ratio, while at the same time Ameren Corp’s more
25 aggressive use of holding company debt has lowered its common equity ratio to 45% from
26 approximately 50% in prior years. Mr. Sagel indicates that on November 9, 2019, Moody’s
27 changed its outlook for the utility industry to “stable” from “negative” as a result of the

²² Sagel Rebuttal, p. 23, l. 15 – p. 24, l. 6.

²³ Id., p. 24, l. 7 – p. 25, l. 10.

1 “implementation of more proactive regulatory and **financial** actions to address sector cash
2 flows following the passage of the TCJA, with regulatory actions including increased
3 authorized equity layers” (emphasis added). While the Commission may certainly be
4 supportive by authorizing a reasonable common equity ratio for ratemaking, it should
5 require Ameren Corp to demonstrate more conservative financial policies before it does
6 so. Instead of being more conservative to promote financial stability since the passage of
7 the TCJA, Ameren Corp has been more aggressive with its use of holding company debt
8 to leverage shareholder returns.

9 **Q. Does the use of holding company debt cause financial instability of the entire family**
10 **of companies?**

11 A. Yes. S&P RatingsDirect is very clear that it does not consider Ameren Missouri as having
12 significant insulation mechanisms in place to allow it to have a separate and distinct credit
13 rating from Ameren Corp. Therefore, Ameren Corp’s financial and business risks impact
14 the rating S&P assigns to Ameren Missouri.

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

18 A. Yes. This was one of the factors cited by the Kansas Corporation Commission’s (KCC) in
19 its disapproval of Great Plains Energy’s proposed acquisition of Westar Energy.

20 **Q. What was the final outcome of the proposed transaction between Great Plains Energy**
21 **and Westar Energy?**

22 A. They restructured the proposed transaction as a merger of equals (“MOE”), which is
23 essentially a transaction in which each company’s shareholders swap their shares for a pro-
24 rated ownership interest in the combined company. Unlike the initial proposed transaction,
25 this type of transaction did not involve use of leverage at the holding company.

1 **Q. Did the KCC impose any conditions on the merger to control the potential of Evergy**
2 **issuing a disproportionate share of holding company debt to leverage its returns after**
3 **the transaction was completed?**

4 A. Yes. A condition of the KCC's approval of the merger was to institute an Earnings Review
5 and Sharing Plan ("ERSP"). The KCC understood that the newly formed entity, Evergy,
6 could attempt to keep more earnings by using more leverage at the holding company level
7 as compared to its subsidiaries. Consequently, to the extent Evergy's consolidated
8 common equity ratio was lower than its subsidiaries' common equity ratios by 2.5% to
9 3.5%, the percentage of equity allowed to be counted for the ERSP would be reduced by a
10 proportionate amount.

11 **Q. How much lower is Ameren Corp's equity ratio compared to Ameren Missouri's**
12 **common equity ratio?**

13 A. Since September 30, 2020, Ameren Corp's equity ratio has been 7.29% to 8.2% lower than
14 Ameren Missouri's common equity ratio.

15 **Q. What common equity ratio did the KCC allow Evergy's subsidiaries for purposes of**
16 **the ERSP?**

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

18 **Q. What common equity ratios has Evergy had over for the past year?**

19 A. Evergy's common equity ratios have been in the range of 47% to 48%.

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

21 A. Around 42% to 43%.

1 **Q. Mr. Sagel takes issue with your suggestion that equity investors now view Ameren as**
2 **a “premium utility,” and whether this resulted in Ameren Corp realizing a lower cost**
3 **of common equity. Do investors view Ameren Corp as a premium utility?**

4 A. Yes. This has been due to a combination of higher expected growth and a lower risk
5 profile. In my Direct Testimony, I provided several examples of equity analysts views of
6 Ameren’s investment profile, which has caused them to assign higher valuation multiples
7 to earnings generated by each of Ameren’s subsidiaries-Ameren Missouri, Ameren Illinois
8 and ATXI.

9 **Q. Mr. Sagel testifies that equity infusions in Ameren Missouri are traceable to Ameren**
10 **external equity issuances, and therefore because this is the capital that supports**
11 **Ameren Missouri’s rate base, this is the capital structure that should be used for the**
12 **authorized ROR.²⁴ First, do you agree that tracing the capital to external issuances**
13 **should be the determining factor of a fair and reasonable capital structure?**

14 A. No. Ameren’s equity issuances benefit the entire family’s credit profile, not just that of
15 Ameren Missouri. A recognized principle of finance is that the source of the funds does
16 not define the cost of capital, the risk of the investment does. Based on Mr. Sagel’s logic,
17 if Ameren Corp only sourced third-party equity for equity infusions into Ameren Missouri,
18 but issued holding company debt to infuse equity into its other subsidiaries, only Ameren
19 Missouri’s capital structure would be legitimate. It is this type of logic that supports S&P’s
20 family ratings approach to assigning credit ratings based on the parent company’s
21 consolidated credit profile.

²⁴ Sagle Rebuttal, p. 9, lns. 14-16.

1 **Q. Mr. Sagel indicates that your direct testimony suggests that Ameren Missouri's**
2 **dividend payout policy should be similar to Ameren Corp's.²⁵ Did he interpret your**
3 **testimony correctly?**

4 A. No. My testimony indicated that if Ameren Missouri were managed as if it were a stand-
5 alone entity, it would have a carefully managed dividend payment policy, similar to how
6 Ameren manages its targeted dividend payout ratio in the range of 55% to 70%.

7 **Q. If Ameren Missouri had been managed as a stand-alone entity, based on Ameren's**
8 **own internal dividend strategy whitepapers, what would its targeted payout ratio**
9 **have been over the last ten years?**

10 A. Being that Ameren Missouri only grew its rate base by 2.2% to 3% over the last ten years,
11 it would only need to retain 68% to 77% of its EPS to have sufficient internal equity capital
12 to fund its investment and maintain a balanced capital structure. Because Ameren Missouri
13 had only been minimally reinvesting in its system, it would have made no sense to retain a
14 higher amount of capital. Therefore, if Ameren Missouri were managed as a stand-alone
15 entity, it would not accumulate excessive amounts of equity as Mr. Sagel suggests because
16 the Company simply wouldn't have the need for retaining this equity. The most
17 appropriate dividend policy for Ameren Missouri over this period would be to target a
18 dividend payout ratio of around 75%.

19 **Q. Doesn't this prove Mr. Sagel's argument that deploying Ameren Missouri's excess**
20 **capital to Ameren Corp's other subsidiaries and for dividend payments to Ameren**
21 **shareholders was an efficient use of capital?**

22 A. Yes. My point was not that Ameren Missouri should retain capital if it is not reinvesting.
23 I was simply indicating that if Ameren Missouri was managed as a stand-alone company
24 responsible to outside investors, these investors would demand a consistent dividend
25 payment with the possibility for a little growth. If this were the case, Ameren Missouri
26 could not pay Ameren Corp \$430 million in dividends in 2019 and then reduce the dividend

²⁵ Sagel Rebuttal, p. 11, ll 12-15

1 payment to \$66 million the very next year (2020). Instead, Ameren Missouri would not
2 only have been required to provide its shareholders a consistent dividend that represented
3 around 75% of its earnings over annual periods, but it would also have been compelled to
4 pay a quarterly dividend consistent with its DPS commitment, which may have required
5 Ameren Missouri to issue short-term debt to fund such dividends during quarters in which
6 there was lower cash available from operations.

7 **Q. Mr. Sagel discusses market responses to the Commission's deliberations in the Spire**
8 **Missouri gas rate cases, GR-2017-0215 and GR-2017-0216, to attempt to justify why**
9 **the Commission should accept Ameren Missouri's proposed capital structure.²⁶ Do**
10 **you think this should be the Commission's primary focus?**

11 **A.** No. While even as a consumer advocate witness, I do consider the potential impact on a
12 company's investors in my recommendations; a negative stock price reaction is not proof
13 of a bad Commission decision. Investors' expectations are impacted by many different
14 factors, with anticipated Commission decisions being one of the primary factors. As I
15 explained in my Direct Testimony, investors price in the probability that utility companies
16 may have their authorized ROEs reduced due to persistently low long-term interest rates.
17 However, the company guidance greatly influences investors' expectations. For example,
18 many companies, including Ameren Corp, provide investors earnings guidance. Ameren
19 Corp has consistently communicated to investors that it expects a long-term CAGR in EPS
20 of approximately 6-8% based on a 2018 normalized EPS. However, this earnings guidance
21 has many assumptions underlying it. The key factors typically influencing the earnings
22 guidance of a pure-play regulated utility such as Ameren are anticipated rate base growth,
23 the probability of recovery of this increased investment, and the parameters applied to the
24 rate base for purposes of allowed returns (which include an assumed capital structure and
25 potential allowed ROEs). ** _____
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28 _____ ** Consequently, to the extent Ameren Corp's earnings guidance

²⁷ Bulkley Rebuttal, p. 11, Ins. 1-4.

1 assumes shareholder friendly regulatory outcomes, it should not be surprising when stock
2 prices react negatively to an outcome that considers ratepayers' interests.

3 **ANN E. BULKLEY'S REBUTTAL TESTIMONY**

4 **Q. What is your response to Ms. Bulkley's view that Ameren Missouri's proposed equity**
5 **ratio is reasonable because it is within the range of authorized equity ratios?²⁷**

6 A. I provided information about authorized equity ratios for other companies in Missouri,
7 which in Evergy Metro's case was consistent with that which the company recommended,
8 and also in Kansas and Illinois. Although a 52% equity ratio may be within average
9 authorized equity ratios, the primary evidence that should be considered is the
10 interrelationship and comparison of Ameren Missouri's capital structure to that of its parent
11 company. Based on this evidence, Ameren Missouri's request equity ratios of ~52% is
12 unreasonable.

13 **Q. Ms. Bulkley claims that you abandoned/discarded your COE estimates for purposes**
14 **of your recommended allowed ROE range of 8.5% to 9.25%, point recommendation**
15 **of 9.0%.²⁸ Is this an accurate representation of your testimony?**

16 A. No. My recommended authorized ROE of 9.0% takes into consideration many different
17 factors. A fundamental principle of shareholder value creation is for a company to invest
18 in projects that allow the company to at least earn its cost of capital. An allowed ROE of
19 9.0% allows for a margin of approximately 225 basis points over my estimate of Ameren
20 Missouri's COE in the range of 6.5% to 7.0%. I am aware investors have become
21 accustomed to regulators allowing utility companies returns that are higher than their cost
22 of capital. In fact, some investors, such as Evercore ISI, use investment models that assume
23 that regulators currently allow an ROE to COE spread of approximately 440 basis points
24 (9.75% ROE – 5.35% COE), but will eventually reduce the spread to a range of 225 to 285

²⁷ Bulkley Rebuttal, p. 11, lns. 1-4.

²⁸ Bulkley Rebuttal, p. 4, lns. 4-8, p. 13, lns. 17-19 and p. 51, lns. 7-9.

1 basis points as either the COE increases, the allowed ROEs decrease or a combination of
2 both.²⁹

3 The fact that the COE for utilities is this low establishes the reasonableness of my
4 recommended authorized ROE, which actually allows Ameren Missouri to increase
5 shareholder value above the classic economically efficient amount, which is at least
6 theoretically supposed to be no greater than the value created from earning a return
7 consistent with the cost of capital. Regardless, my determination that the COE is much
8 lower than Ameren Missouri's last authorized ROE of 9.53% provides support for reducing
9 Ameren Missouri's authorized ROE. However, I also understand from past Commission
10 decisions that the Commission has set a zone of reasonableness ("ZOR") that has generally
11 been 100 basis points (1%) above and below recent average authorized ROEs. Recent
12 average authorized ROEs have been around 9.5% or a bit lower. Therefore, this established
13 the low end of my recommended authorized ROE range because the Commission has
14 indicated it won't consider anything below this level.

15 **Q. Ms. Bulkley suggests that you should have reconsidered the validity of the inputs and**
16 **assumptions you used in your analysis considering your COE estimates are so much**
17 **lower than the average level of ROEs authorized around the country.³⁰ What appears**
18 **to be the underlying assumption that Ms. Bulkley considers fact when making this**
19 **criticism?**

20 **A.** Ms. Bulkley's position assumes that commission authorized ROEs reflect investors'
21 required returns for providing utilities' equity capital. I do not agree with Ms. Bulkley.
22 More importantly, investors do not agree with Ms. Bulkley. However, I do agree that
23 investors expect commissions to continue to authorize ROEs higher than the COE.

²⁹ Durgesh Chopra and Michael Lonagan, "On the Heels of Deals, A Look at Utilities M&A" Evercore ISI, October 31, 2021, p. 5.

³⁰ Bulkley Rebuttal, p. 15, ll. 12-14.

1 | **Q. Following Ms. Bulkley's logic related to her testimony that because authorized ROEs**
2 | **are so much higher than your COE estimates, do you have any suggestions for Ms.**
3 | **Bulkley for purposes of testing the reasonableness of her inputs and assumptions?**

4 | A Yes. I'd suggest she review the specific utility investor reports I reviewed to determine the
5 | assumptions they used when valuing utility stocks. I also suggest that she review Ameren
6 | Corp's own internal materials which discuss inputs and assumptions Ameren Corp
7 | consider reasonable when analyzing dividend strategies and capital structure management.

8 | **Q. Ms. Bulkley claims that you are incorrect in stating that investors expect authorized**
9 | **ROEs to be at risk due to continued low long-term interest rates. Did you provide**
10 | **corroborating investment materials to support your position?**

11 | A. Yes. I provided information from Evercore ISI and Wells Fargo.

12 | **Q. Did Ms. Bulkley provide corroborating support for her testimony that investors do**
13 | **not expect authorized ROEs to decline?**

14 | A. No. In response to OPC Data Request No. 3016, Ms. Bulkley indicated her testimony is
15 | based on her observations related to the typical correlation of utility stock valuations as it
16 | relates to changes in interest rates. Of course, her position assumes that projected increases
17 | in long-term interest rates aren't already factored into the price investors are willing to pay
18 | for utility stocks. The key determining factor of whether utility stock valuation levels will
19 | increase or decrease from current levels is not whether interest rates will increase, but
20 | whether they will be different from investors' expectations.

21 | **Q. What do you mean?**

22 | A. Current utility stock prices already reflect investors' expectations on potential changes in
23 | long-term rates. While it is fairly difficult to agree on the actual consensus expected long-
24 | term rate factored into current utility stock prices, investors are factoring in increases in
25 | long-term rates. For example, JP Morgan's recent regression analysis of utility forward
26 | P/E ratios to 10-year United States Treasury ("UST") yields indicates that current utility
27 | stock prices imply investors are factoring in a forward yield on the 10-year UST of

1 approximately 5%.³¹ This compares to the recent current 10-year UST yield of
2 approximately 1.6%. Based on JP Morgan's analysis, if 10-year UST yields increase to
3 less than 5%, this could allow for further expansion in utility P/E ratios, which is contrary
4 to Ms. Bulkley's views.

5 **Q. Does Ameren Missouri's own witness, Mr. Sagel, question anyone's ability to have**
6 **the foreknowledge to accurately predict changes in interest rates?**

7 A. Yes. Mr. Sagel claimed I do not have foreknowledge of interest rate changes and corporate
8 debt markets over the next 10 to 30 years, a claim I do not dispute.³² Consequently, I asked
9 him if he was aware of anyone that he trusts to have this foreknowledge. He indicated he
10 is "not aware of any individual with such foreknowledge." Mr. Sagel's statement is
11 consistent with the efficient market hypothesis which dictates that current security prices,
12 including UST bonds, reflect all potential changes in economic, monetary and fiscal policy
13 changes in the future.

14 **Q. What is the relevance of these issues as it relates to Ms. Bulkley's rebuttal testimony?**

15 A. Ms. Bulkley appears to believe she has foreknowledge that isn't already priced into current
16 security prices. This forms the basis for her opinion that a DCF analysis underestimates
17 the cost of equity. It also forms the basis for her decision to use projected interest rates in
18 her CAPM and Bond Yield Plus Risk Premium (BYPRP) analysis. She claims that these
19 are factors that explain why my COE estimates are unreasonably low.

³¹ Jeremy Tonet, CFA, et. al., "North American Utilities – Thoughts Into 3Q Earnings: Summer Breeze Makes 3Q
Feel Fine," October 21, 2021, p. 6.

³² Sagel Rebuttal, p. 27, lns. 16-19.

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