— BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH —

IN THE MATTER OF THE APPLICATION OF QUESTAR GAS COMPANY FOR A GENERAL INCREASE IN RATES AND CHARGES	)))))))	**Docket No. 02-057-02**

POST-HEARING REPLY BRIEF OF QUESTAR GAS COMPANY

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Pursuant to the briefing schedule established by the Commission at the close of the hearings on October 21, 2002, Questar Gas Company (QGC or the Company) respectfully submits its Post-Hearing Reply Brief in response to the briefs filed by the Division of Public Utilities (Division), the Committee of Consumer Services (Committee), the Utah Association of Energy Users (UAE) and the Salt Lake Community Action Program et al. (SLCAP).

Rate of Return on Equity Capital (ROE).

Introduction. When reduced to its basic elements, the theme in the post-hearing briefs of both the Division and the Committee is that the Commission's ROE authorization in Docket No. 99-057-20 of 11.0% should serve as the "starting point" for deciding the ROE issue in this case. Although the briefs discuss the evidence in some measure, the thrust is: 11.0% was good enough two years ago in Docket No. 99-057-20; nothing catastrophic has happened since then; therefore, the proper ROE in this case can't be any more than 11.0%

This syllogism is flatly wrong—for at least two reasons. (a) The basic evidence and data that is before the Commission in this case is substantially different from the information on which the Commission based its decision in the case filed at the end of 1999, and the analysis must be based on *this* evidence. (b) The 11.0% set by the Commission two years ago was demonstrably too low then and it is even more clearly too low today.

Although prior orders of the Commission often play an important role in subsequent proceedings, the primary factual analysis must be to examine and carefully analyze the evidence and arguments in this case on their merits and resolve the issues directly from that information. To be sure, the Commission often must either harmonize a decision with previously stated fundamental principles or explain the basis for its departure. But, on the ROE issue, the Division and Committee would have the Commission minimize the compelling current evidence and focus on results from two years ago.

This is today's case; it is to be decided—both legally and equitably—on the evidence in the present record. And the present record contains persuasive evidence that the cost of equity capital in today's financial marketplaces is significantly more than the 11% the Committee and Division wish were the upper limit, and even more clearly in excess of the 10.0% and 10.5% levels they recommend.

The Central Role of the Dividend Growth Issue. When all of the rhetoric, posturing and verbal underbrush is cleared away, the major issue that faces the Commission in its task to sort out the ROE issue is to determine the role of dividend growth in applying discounted cash flow models.[1] This is pointedly illustrated by Dr. Powell's Exhibit DPU 6.3, on which is displayed the central figure in this controversy: **7.21%** is Dr. Powell's estimate of the cost of equity capital for Questar Gas Company when dividend growth estimates provided by *Value Line* forecasters[2] "drive" the standard DCF model.

The key evidence on this issue is the changing role of dividend growth and the corresponding projections in the eyes of investors—evidence that has been building for some time. It was present to some degree in the last QGC case. Indeed, to the extent the Commission's final ROE determination in that case adopted Dr. Powell's 11.0% recommendation, the dependence on dividend growth information essentially reduced these to 25% in the ROE calculus. (25% DCF-earnings, 25% DCF-dividends, 50% for two TVM models, Tr. 510-11.)

There is uniform agreement that the dividend growth rates by themselves do not produce return estimates that would attract any rational investor when that rational investor could put his capital into "A" and "Aa" utility bonds at far less risk. From here, however, the witnesses went in two different directions. Professor Williamson concluded that dividend growth rates do not provide reliable inputs to the DCF and he discarded them. But, in the face of these red flags, the Division and Committee

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[1]The term "discounted cash flow" is used here in its "lower case" sense. That is, it includes both the infinite-horizon model, which is most often designated as *the* DCF model, as well as finite-horizon models such as the TVM (terminal value model) used by Dr. Powell. (*See, e.g.,* Tr. 456-58.)

[2]Recall that there is only one *Value Line* forecaster for each proxy company.

witnesses nevertheless pressed ahead with the dividend growth information and folded it into their applications of the DCF model. As Professor Williamson pointed out, "There is a widespread fallacy that no matter how absurd the result of a particular methodology, so long as that result is averaged in with other results to reach a final recommendation it is not objectionable." (Exh. QGC 3.0R, at 25.)

Both direct and indirect evidence was presented in this case to show the near-total unreliability of dividend growth information for determining plausible ROEs; this mandates either eliminating or minimizing the use of dividend growth information. From a direct perspective, there are the commentaries of Chairman Greenspan and Professor Williamson, as well as the increasing divergence of dividend and earnings growth data and projections.[3] Indirect evidence is found in the simple fact that the use of dividend growth projections produces quite outlandish estimates of ROE.

To focus the inquiry even more narrowly, the key question is: Can 7.21% represent a *bona fide* estimate of the cost of equity, to be legitimately included in the final analysis and determination of ROE for QGC?[4] There are three possible responses to

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[3]See Questar Brief at 7-9.

[4]Mr. Parcell's DCF calculations produce even lower values than 7.21% when dividend forecasts are used. For example, the "DPS" [dividend per share] columns of Parcell's Exhibit CCS 4.7, page 3, yield equally implausible ROEs. For his *Value Line* Group, the average historic and projected DPS values that he incorporates in his final calculations yield:

4.8% (*D/P* from page 4) + [2.1% + 1.7%] ÷ 2 (ave. for DPS from page 3) = **6.7**%

—a value that is even more preposterous than Dr. Powell's 7.21%.

this question:

(1) Yes. This is the answer given by the Division and Committee and its witnesses: Numbers such as 7.21% are fully legitimate estimates of the cost of equity capital for QGC and should be directly averaged with values obtained from other data and procedures. This inherently depends on the related, and indefensible, claims that 7.21% is a "lower bound" for investors' expectations, and that 7.21% is not an "outlier" among the various other ROE estimates. This position is simply untenable. It is not a rational interpretation of the evidence in this case and should be summarily rejected.

(2) No. It is impossible to postulate that there are rational investors who view 7.21% as a plausible expected return on equity capital they are asked to commit to a company like QGC. Accordingly, the DCF analyses should not include any such anomalous numbers. This is the perfectly reasonable and supportable view advanced by Professor Williamson to derive 12.60% (updated later to 12.47%) as the cost of capital for QGC. It is completely consistent with the demonstrated inapplicability of dividend growth rates in the DCF model in today's investment environment and with all three witnesses' analysis for the nine proxy companies[5] when the downward-biasing effects of dividend growth projections are removed.

(3) No, but the Commission is reluctant to abandon completely its past practice of incorporating information about dividend growth projections in the application of the DCF model. Accordingly, it would consider adopting, for this case, an analysis that substantially reduces the weight given to the dividend-growth information, recognizing:

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[5]The proxy group that was used by all three witnesses.

(i) investors' diminishing reliance on dividend growth to estimate the equity returns they seek, and (ii) the widening divergence between dividend and earnings growth estimates.

This last conclusion is a rational view that arguably provides a smooth transition from recent approaches to the ROE issue while taking account of the increasing unreliability of dividend growth forecasts as DCF inputs.[6] Although QGC believes the evidence against using dividend growth estimates in the DCF model is compelling, a major reduction in the weighting of this information would go far in rectifying a problem that has been developing over several years.

Dr. Powell's TVM as a Reasonableness Check. The increasing divergence of dividend and earnings growth rate information may lead the Commission to the conclusion that, under today's conditions, it may be prudent to turn to other methods to supplement the constant-growth (infinite horizon) form of discounted cash flow analysis. Dr. Powell's TVM, while not a be-all, end-all for the issue, is one such alternative to address current conditions. As he explained, it is a finite-horizon cash-flow method, and

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[6] Incidentally, the Committee's and Division's Briefs confuse investors' continued interest in steady dividend payments with their rejection of dividend-growth forecasts as an element that influences their return expectations. Compare, for example, Committee Brief at page 17 and Division Brief at 11-12 with Professor Williamson's discussion, Tr. 328-29. "No, I didn't say they don't look at dividends anymore. They don't consider dividend *growth rates* to be important. If they did, analysts would be providing dividend growth rates, and they don't. Only *Value Line* does." (Emphasis added.) Interest in stocks that pay steady dividends has little to do with whether dividend growth rate forecasts are appropriate inputs to the DCF model.

it does not rely on the suspect dividend-growth projections, nor on assumptions that all dividends, earnings and book values grow at the same constant rate into the indefinite future. (Tr. 456-60.) Rather, it merely looks five years into the future (in Dr. Powell's analysis) and combines expected dividend payments with the expected price of the common stock of the company.[7]

Most importantly, under the circumstances that currently face the Company and the Commission, this method provides a plausible alternative that avoids the contentious analysis of outliers, box plots, median-v.-mean, and the hotly contested role of dividend growth rates. From Exh. DPU 6.3, Dr. Powell's TVM analyses provides the following ROE estimates:

	Mean	*Median*
TVM with current P/E ratios	11.87%	11.07%
TVM with forecasted P/Es	12.74%	13.16%

These values are consistent with and tend to corroborate the ROE estimates made by

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[7]According to Dr. Powell:

> By employing what I call the TVM model, yes, you do get what I refer to as a terminal price, what the price of the stock that you expect five years out based on Value Line's data. But in order to be consistent with the DCF model, which you are assuming, is that terminal price is itself the discounted cash flow, the present value of an infinite stream of income into the future. So I'm not making any guesses about beyond five years, but the model still imbeds the basic discounted cash flow idea. And that is that the current price is equal to the discounted cash flow of an infinite stream.

Professor Williamson—particularly the means that Dr. Powell uses in this case .

Is this discussion an abandonment by the Company of Professor Williamson's analysis, which does not use the TVM? Certainly not. It merely highlights that, when the Division witness's analysis is examined carefully, it has all the ingredients that confirm Professor Williamson's recommendation, once the 7.21% outlier value is recognized for what it is—an anomalous result that does not measure investors' expectations.

One final way to look at the TVM results: If these are considered as a "check" on the reasonableness of other model results, they convincingly *fail* to confirm Powell's and Parcell's dividend-driven DCF results as reasonable estimates and concurrently confirm Professor Williamson's results as well as Dr. Powell's other earnings-based DCF results.

This analysis is also consistent with the development in QGC's initial brief that followed the questions from Commissioner Campbell concerning a weighting of the dividend and earnings growth information on the basis of the number of different analysts that provided the information.[8] Extending Dr. Powell's weighting technique in this fashion produces a cost of capital estimate of 11.83%.[9]

Docket No. 99-057-20 ROE Does Not Serve as a Starting Point in this Case. The Division and Committee pin much of their argument on the Commission's establishment

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Tr. 460.

[8]A technique used by Dr. Powell in his "DCF w/weighted earnings" derivation.

[9]See QGC Brief, at 15-16, for the full development. (Correction: The docket reference on page 15, line 7, of the QGC Brief should be to Dr. Powell's weighting in Docket No. *99-057-20*, not to Docket No. 02-057-02.)

of 11.0% as the proper ROE in QGC's last general rate proceeding and then proceed to peck away at it by claiming, somewhat hyperbolically, that QGC is so much better off now than it was two years ago.

This approach is attractive to the Division and Committee because it minimizes—if not ignores—major evidentiary developments since that time, as discussed in detail in the previous section. Contrary to the implication that "nothing has changed," a great deal has changed, and the Commission's responsibility is to take the complete record in this case and evaluate it on its own merits. History is not necessarily irrelevant, but a fixation on the value set two years ago cannot be the basis for sound decision-making.

Beyond that, there is the issue of whether the 11.0% established in that case was a reasonable level. QGC believes that 11.0% was an illusory target that the Company had no chance to achieve from the outset. It has not been contested on this record that the Company has fallen substantially short of the value set by the Commission in the last case.[10] And the reasons for this shortfall were not due to random or supervening events, but were systemic in nature.

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[10]As Mr. Allred testified:

> But for Questar Gas, the most serious situation we face is since the last rate case, even with the significant revenue increase from the last rate case and further significant effect—impacts or actions taken by the company to lower costs through an early retirement program by about 5 million dollars a year, . . . the actual returns we've been able to provide investors have not risen above the *nine percent level.*

Tr. 145-46 (emphasis added).

The use of an average historical test year in that case led to the Company's inability to absorb the devastating effects of declining per-customer usage and the inexorable rise in the Company's rate base. It pre-ordained the Company's failure to achieve the ROE set by the Commission—even in the face of some $5 million annual savings from an early-retirement program that was implemented when drastic steps became necessary to protect the financial health of the Company.

Approval of the Revenue Requirement Stipulation and Settlement in this case will significantly mitigate, but not entirely solve, this fundamental problem. Even if the test-year treatment in the Settlement were to be adopted as ongoing policy by the Commission, it only brings QGC into the same arena that the rest of the LDCs in the United States have already been in. (*E.g.*, Tr. 130-31, 201.) And there is still major exposure to the ravages of decreasing usage per customer and increasing requirements for new investment during the rate-effective period.[11]

Mr. Allred's Exh. QGC 1.12R quantitatively illustrates the effect of the ratemaking process's inability to keep up with events. In a three-year period from 1999-2001, the difference between actual average usage per customer and the per-customer usage incorporated in rates produced a shortfall in Company revenues averaging over $10 million per year. To the extent that average usage per customer continues to fall below the level to be reported to the Commission in December 2002, the exposure of the

[11]To the extent that the Commission declines to articulate a *policy* concerning the use of a projected or future test year or other means of matching rate conditions with the rate-effective period, QGC will be faced with the same problems and regulatory risks when its next case is filed.

Company to this kind of shortfall still exists. This is a clear and present risk to the Company.

The point is that an authorized return of 11.0% two years ago was inadequate then, and it is inadequate now.

The Moody's Credit Downgrade. There may have been the tendency in some quarters to regard the Company's past and current claims of possible credit downgrades, with the corresponding tangible effect of an increase in QGC's cost of debt, as merely an overly dramatic, exaggerated exercise. Unfortunately, the facts are to the contrary. As was discussed at some length during the hearings, the Company's credit rating was then being evaluated by Moody's Investors Services. (*E.g.*, Tr. 252-53.) On November 12, shortly after the close of the hearings, Moody's issued its credit report for Questar Corporation and its subsidiaries, including Questar Gas Company. The report announced that Moody's had downgraded the senior unsecured debt rating of Questar Gas Company from A1 to A2.[12] The relevant portion of the report reads:

> The A2 rating of Questar Gas (25% of last twelve months' operating income as of September 30) reflects returns that are below its authorized returns and also the industry average; it also reflects weak earnings coverages. However, it has maintained leverage at about 50%, in line with industry norms and at about its

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[12]As a document issued by one of the two well-known bond rating agencies and containing information relevant to the ROE issue in this case, QGC moves for admission, as a late-filed exhibit, the four-page document issued by Moody's Investors Service, entitled "Rating Action: Questar Corporation," and dated November 12, 2002. The report was filed with the Commission and served on the parties by letter dated November 13, 2002. A copy marked Exhibit QGC Late-filed-1 has been included with this Reply Brief as Appendix 1.

> allowed equity ratio. Questar Gas is relatively mature compared to its sister companies. Nevertheless, it has a higher customer growth rate than the average US gas distribution company. Although the growth is moderating, it has made regulatory lag a persistent issue, its return-on-equity was 9% for the last twelve months ended September 30, well below its 11% authorized return and average for the industry. It has filed for a general rate increase in Utah with settlement expected to be announced in the near-term. We assume in our rating that the settlement results in a revenue increase that would at minimum help to prevent a further weakening in its returns and coverages (EBIT/interest at 2.8 times for the last twelve months ended September 30).

This is important evidence to show that one of the two major rating agencies considers the actual returns being generated by QGC's utility operations to be inadequate to support its then-current rating.

In that regard, the Division has quite properly noted that "The Company is entitled to a return that will allow it to maintain its credit." (DPU Brief at 2.) But, that's not what has taken place as result of the outcome in Docket No. 99-057-20. The upshot of Moody's action is that the Company's previously authorized return did *not* "allow it to maintain its credit."

As Mr. Rattie testified, the QGC credit rating is still under scrutiny by the other major bond-rating agency, Standard & Poor's.[13] It is notable that S & P has

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[13]Mr. Rattie testified:

> Standard and Poor's is looking at the totality of management's actions, and they see us taking aggressive action to protect our credit rating, so as a consequence, they've recently affirmed the current ratings. They still have a negative outlook on the company, but they're saying, "Management's. . . on top of this. They're making some . . . moves that directionally are good with respect to the credit ratings. We're going to keep watching them, but we see no need for action right now."

characterized QGC's credit as having a negative outlook since prior to the last general rate proceeding, and the final order in that proceeding in August 2000 did *not* persuade S & P to remove the negative outlook designation—a cloud QGC continues to operate under. The Company fears that a Commission order that does not fairly recognize QGC's true cost of capital could induce S & P to follow Moody's lead on this issue. No one would benefit from such an action—neither the Company's owners nor its customers. A failure to significantly increase QGC's ROE will, as the Company's witnesses have testified, send a message to the investment community that may lead to unwanted consequences in QGC's efforts to function as effectively and economically as in the past.

The important conclusion from the discussion in these last two sections is that it is not particularly relevant whether 11.0% was right or wrong last time. The Commission established it; the Company struggled to meet it by making drastic cost reductions; it actually earned only in the single digits; Moody's downgraded QGC's debt rating. But we are here with an entirely new and complete evidentiary record that addresses *today's* conditions, not August 2000's.

Misrepresentation of QGC's ROE Position. Although a relatively harmless distortion, the parties have chosen to characterize 11.75% as a new ROE point recommendation put forward by the Company.[14] It is neither that nor an evidentiary

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Tr. 277.

[14]DPU Brief at 5, CCS Brief at 4-5, UAE Brief at 4. The UAE Brief has the temerity to manufacture a "range of possible returns" by elevating QGC counsel's 11.75% example to the status of an

value. The only place this number appears in the record is in the context of a statement by counsel concerning the Company's recognition of an improvement in the regulatory-lag problems facing the Company relative to the time when Professor Williamson conducted his ROE analysis.[15]

Parties have seized on the Company's recognition of the changed circumstances over the course of the proceeding and its acknowledgment that there has been regulatory-lag mitigation. They complain that it is a "moving target," that there was a last-minute change of position, and that the 11.75% cited as an example by counsel has become an evidentiary position that replaces Professor Williamson's well-grounded 12.6%. None of this has the slightest relevance, importance or merit.

First, the record evidence—Professor Williamson's, e.g.—is what must form the basis for the Commission's conclusions on this fact-intensive issue, not numbers that counsel states as examples to illustrate a position. Further, the applicant in a case of this kind is quite clearly within its rights to suggest that mitigating circumstances may have developed that would not require an ROE award at the exact number that its expert witness had proposed several months earlier. After all, there is credible evidence

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evidentiary recommendation and proclaiming a neither-fish-nor-fowl result that has no merit whatsoever. The "range" of witnesses' *evidence* is still 10.0% (Parcell) to 12.6% (Williamson).

[15]By Mr. Sackett: "And just to give you some perspective on the size if, for example—pick something as an example only—[t]he rate of return of 11.75 percent were to be looked at in place of 12.6 percent, that actually reduces the revenue requirement by about 4 million dollars per year." (Tr. 528.)

encompassing ROEs that are somewhat lower than 12.6%—even among Professor Williamson's results.[16]

These parties' responses to the Company's position was predictable. The very existence of the Revenue Requirement Stipulation and Settlement had put them in a no-lose position with respect to this argument. If the Company stubbornly refused to acknowledge that the Stipulation provides a more favorable regulatory-lag situation than it had previously experienced, there would be a barrage of criticism from the parties rebuking the Company for not recognizing the positive effects of the changed circumstances.

When the Company stepped forward and acknowledged the salutary regulatory-risk effects of the Stipulation and conceded that this development could justify a slightly lower ROE than it originally proposed, up jumped the parties with a variety of lamentations and allegations: It's a moving target; it's too late; it proves that the current ROE should be whacked; the Company has abandoned its witness's evidence; etc. None of this goes to the merits of the actual record evidence. To paraphrase a well-known frog: It's sometimes not easy being a utility company.

Recent Commission Decisions on ROE. At pages 9-10 of its Brief, the Committee takes issue with the information that the Company has provided on recent return-on-equity results from utility commissions around the country. The information about authorized ROEs in Exh. QGC 1.13R was, to the best of the Company's ability and

[16]This is not a "baseball arbitration" process, where side *A* provides one number, side *B* another, and the arbitrator is required to choose one or the other, but not something in between.

knowledge, complete and not selective in any way[17] and was provided during the hearings when all parties had every opportunity to cross-examine the Company witnesses on the information or to present counter-evidence of their own. No party took such action. With respect to the information about actual earned returns that was provided in Exh. 2nd Rev. Exh. QGC 1.13R, this information was provided in response to a request by the Commission (Tr. 439-40) near the conclusion of the hearings.[18] No

[17]"I included every case I was aware of that I could find in the reports where an actual return-on-equity finding was made either by stipulation or by Commission decision." (Mr. Allred, Tr. 234). Until Mr. Parcell brought up the Chesapeake Utilities case in his testimony, it had escaped everyone's notice, including the compilers of the 2002 *Public Utilities Fortnightly* ROE list. (*See* Exhs. DPU Cross-5 and Cross-6.) It is included in the supplemental information in note , *infra.*

[18]To bring the ROE information as up-to-date as possible, QGC can report the following additional results from recent published opinions. As far as Company personnel can determine, this list is exhaustive. (It does not report results in which a commission order does not explicitly cite the equity return implicitly incorporated in the utility's rates, such as the Southwest Gas "black box" case claimed by Mr. Parcell in his affidavit. *See* Tr. 390-91.)

Date	*CompanyDocket*	*Agency*		*Auth. ROE*
04/16/02	Chesapeake Utilities	01-307	Delaware PSC	10.86%
10/28/02	Piedmont Natural Gas	G-9, Sub 461	North Carolina Utilities Comm.	11.3%
11/01/02	Piedmont Natural Gas	2002-63-G	PSC of South Carolina	12.6%
11/07/02	Consumers Energy	U-13000	Michigan PSC	11.4%
11/08/02	MidAmerican Energy	RPU-02-2	Iowa Dept. of Commerce Board	10.75%

party has sought to submit information that would refute the data in the Company's filing.

The information in the 1.13R exhibit may not directly establish the exact value of ROE for QGC, but—in the way that every ROE witness looks at reasonableness checks for their primary methods—it provides a very persuasive check that ROEs in the "high 11s" and "low 12s" are clearly within a reasonable range for a gas utility in today's environment, *and 10.0% and 10.5% are not even close*.

Minor ROE Issues.

The Public Utilities Fortnightly *Compilations.* The Committee's brief points to a headline in Exh. Cross-5, from the December 2001 issue of the *Public Utilities Fortnightly* as an indication that utility ROEs are headed down. The actual numbers in the table don't support the headline, but, more to the point, this compilation is *more than a year out of date* and tells the Commission nothing about the most recent authorized ROE levels. Recent information from at least two sources is far more indicative of current commission actions. If the data in Appendix A to QGC's initial brief (Exh. 2nd Rev. QGC 1.13R) are augmented by the information in footnote 18 of this Reply Brief, the results shown in Appendix A change very little—mean value of 11.56% and median of 11.25%.

In addition, the November 15, 2002, issue of the *Public Utilities Fortnightly* (Exh. DPU Cross-5) provides a compilation through approximately September 2002 that exhibits results similar to those in Exh. 1.13R. Exh. DPU Cross-6 sets out the 26 gas cases listed in the 2002 *Fortnightly* article and shows the mean of gas utility results to be 11.30%; the median is 11.25%.

Proxy companies. The Committee and Division Briefs suggest that the inclusion of Questar Corporation and National Fuel Gas Company in Professor Williamson's set of proxy companies substantially "skews" the estimate of ROE. First, the Division's witness performed his basic analysis on the same nine companies, and the Committee's witness also used the same companies as one of his proxy groups.[19] It seems odd now to claim there are companies that don't belong. More importantly, the differences between the results obtained by removing these two companies is relatively small, as Professor Williamson testified concerning Exh. Cross-9.[20] Questar and National Fuel Gas in or out? It's an issue where there are reasonable arguments on both sides, but on the facts of this case, it is a very minor issue.

Median v. mean. The Division brief (page 13) suggests that Professor Williamson's use of medians in his analysis produces a material flaw in the outcome. Except for the fundamental problem of Dr. Powell's 7.21% outlier estimate discussed in

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[19]And, as noted in QGC's opening brief (at pages 18, 20), Mr. Parcell did not perform any direct analysis to "qualify" companies for any of his three groups.

[20]Professor Williamson testified:

> It makes rather little difference. If you're working with the means, the number would come down by 27 basis points, and if you're working with the medians, it would come down by 19 basis points, which I think is a -- considering the accuracy of any estimate of rate of return, those are pretty small numbers.
>
> So as a practical matter, it doesn't really matter whether you put Questar in or whether you put National Fuel Gas in.

(Tr. 364-65.)

substantial detail above in this Brief, the question of mean versus median is really a nonissue in this case. The various compilations of statistics and model results that display both means and medians produce results that do not differ materially. This is just not a large issue. If the "7.21 problem" is taken care of (either by declaring it an outlier or by recognizing this as the one place where the median must be taken instead of the mean), there is not a dime's worth of difference overall.

Capital Structure.

The Committee's Brief raises no major arguments for its proposal to ascribe a 2.27% interest-cost rate to 10% of the investment that supports the Company's rate base that were not addressed in QGC's opening brief,[21] and QGC will respond to the Committee brief on this subject by reviewing the evidence on this issue:

1. Professor Williamson set the foundational utility-theoretic framework that the capital structure consists of the capital the utility company dedicates to obtain the assets that constitute the rate base. (Exh. QGC 3.0R, at 4-6.)

2. The rate base consists of those permanent assets dedicated to providing utility service and excludes, among other major expenditures, the funds necessary to finance construction work in progress and purchase of gas supplies. The inner workings of the various assets that require financing were given in extensive detail by Mr. Curtis. (Tr. 371-73.)

3. Mr. Curtis also provided a detailed explanation and a table (Exh. QGC 7.0R, at 11) to show that the value of rate base and the sum of long-term debt plus equity

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[21]*See* QGC Brief at 22-29.

match very closely, and that short-term debt, indeed, often has a short-term life that is dependent on the ebb and flow of purchased-gas costs and incoming revenues. In particular, the wide-swinging dynamics of the gas-purchase and gas-revenue process can only be dealt with by short-term financing.

4. Further, Mr. Curtis's Exh. 7.3R demonstrates that short-term debt generally tracks the CWIP and gas purchase levels and is not related to permanent assets.[22]

5. On the other hand, in support of including short-term debt in QGC's capital structure, the Committee offers no more than: (a) QGC uses short-term debt for some purposes, and (b) there are other companies whose regulatory capital structures include some unspecified short-term debt for unspecified purposes. In contrast to Mr. Curtis's extensive evidence, Mr. Parcell conducted no study or analysis of the Company's overall need for different kinds of capital, including the need to finance gas purchases and CWIP, which are not part of the rate base. There simply isn't any Questar-specific evidence to establish that short-term debt finances any part of rate base; the evidence is precisely to the contrary.

Conclusion.

For the reasons given above and in its initial Post-Hearing Brief, Questar Gas

[22]That the level of short-term debt exceeded CWIP plus gas-balance levels for a short time in 2000-2001 actually bolsters the position that the borrowing is, in fact, "short term." The divergence was caused by the temporary run-up in gas costs that required extraordinary levels of very short-term borrowings. That temporarily high need has receded as gas costs came back down and stabilized. (*E.g.*, Tr. 371.)

Company requests that Commission:

(a) Admit into the record the Moody's report marked as Exhibit QGC Late-filed-1 and attached as Appendix A;

(b) Adopt QGC's actual capital structure in the determination of the overall rate of return on rate base, rejecting the capital-structure proposal of the Committee;

(c) Authorize the Company to file rates and charges based on a return on equity that is consistent with the testimony and evidence of Questar Gas Company witness and the arguments set forth in this Reply Brief and the company's initial brief.

RESPECTFULLY SUBMITTED this 25th day of November 2002.

QUESTAR GAS COMPANY

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QUESTAR CORPORATION

Exhibit QGC Late-Filed 1

Moody's Investors Service
Questar Corporation
Ration Action November 12, 2002

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing Post-Hearing Reply Brief of Questar Gas Company was mailed, postage prepaid, this ___ day of November, 2002 to the following:

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