

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

IN THE MATTER OF THE APPLICATION
OF QUESTAR GAS COMPANY TO
INCREASE DISTRIBUTION NON-GAS
RATES AND CHARGES AND MAKE
TARIFF MODIFICATIONS

Docket No. 07-057-13

RATE OF RETURN REBUTTAL TESTIMONY OF

ALAN K. ALLRED

FOR

QUESTAR GAS COMPANY

April 28, 2008

QGC Exhibit 2.0R (ROR)

2 **Q. Are you the same Alan K. Allred who previously filed Direct Testimony in this**
3 **proceeding?**

4 A. Yes, I am.

5 **Q. Please state the purpose of your Rate of Return Rebuttal Testimony.**

6 A. The purpose of my Rate of Return Rebuttal Testimony is to respond to the unreasonably
7 low rate of return on equity (ROE) recommendations of the Division of Public Utilities
8 (Division) and the Committee of Consumer Services (Committee) filed in this case and to
9 show that the recommendations, if approved, will seriously jeopardize the ability of
10 Questar Gas Company (Questar Gas or Company) to provide reliable, safe and adequate
11 service to our customers.

12 **Q. Is Questar Gas' ability to serve customers linked to providing investors a sufficient**
13 **and fair return?**

14 A. Yes. As I stated in my direct testimony

15 The growth in the number of customers and the corresponding growth in
16 peak-day demand, along with maintaining our infrastructure requires
17 annual capital investment of \$130-\$140 million. Investors require a
18 sufficient and fair return in order to provide the needed capital. Without
19 an adequate rate of return, we cannot meet our customers' or our
20 shareholders' expectations. Our customers expect and are entitled to safe
21 adequate, reasonably-priced natural gas service. Our shareholders expect
22 and are entitled to a sufficient and fair rate of return. The continued
23 success of Questar Gas requires meeting both expectations. (QGC Exhibit
24 2.0, lines 11-18.)

25 The \$130-\$140 million annual capital investment required to meet customer growth and
26 maintain the ability of the distribution system to meet customers' natural gas demand in
27 an adequate, safe and reliable manner exceeds the level of internally generated funds.
28 Questar Gas had to raise new capital this year and will have to regularly raise new capital
29 in future years. Thus, the determination of the allowed ROE by the Commission in this
30 proceeding is not an academic exercise. It will be a key determinant of Questar Gas' cost
31 and availability of capital.

32 Just, adequate and reasonable rates require maintaining the financial integrity of the
33 utility by assuring a sufficient and fair rate of return and protecting the long-range interest
34 of customers in obtaining continued quality and adequate levels of service. (See Utah
35 Code Ann. § 54-4a-6(4).)

36 **Q. Do the Division's and Committee's allowed ROE recommendations strike this**
37 **balance?**

38 A. No. Their 9.25% and 9.0% recommendations are far too low. If the Commission adopts
39 either of these recommendations, Questar Gas will not be able to provide equity investors
40 a sufficient or fair return. Despite Questar Gas' best efforts, allowed ROEs at these low
41 levels will negatively impact our ability to provide customers with adequate, safe and
42 reliable utility service at reasonable rates.

43 **Q. Are the Division's and Committee's recommended allowed ROEs below the allowed**
44 **ROEs of other gas LDCs?**

45 A. Yes. As shown in Mr. Hevert's Chart 1 on page 8 of his Rate of Return Rebuttal
46 Testimony, the Division's recommendation of 9.25% and the Committee's
47 recommendation of 9.0% are at or below the bottom of the range of recently allowed
48 returns granted by other state commissions for gas utilities. Commission adoption of the
49 Division's or Committee's recommendation will send a powerful message to investors to
50 take their capital elsewhere.

51 **Q. What question will investors ask if the Commission adopts the Division's or**
52 **Committee's recommendation?**

53 A. The basic question will be "why should I invest in Questar Gas with an allowed ROE of
54 either 9.0% or 9.25% when I can invest in natural gas public utilities in other states with
55 significantly higher returns?" Looking at Mr. Hevert's QGC Exhibit 3.1R, potential
56 investors in natural gas public utilities could put their money to work in Wisconsin gas
57 utilities with an allowed return of 10.75% determined by the Wisconsin Commission in

58 January of this year.¹ Investors are not just limited to gas utilities with recent allowed
59 ROE determinations. Investors could also put their capital to work in a California gas
60 utility that has a gas-cost pass-through mechanism, effective decoupling, biannual rate
61 adjustments for O&M costs and for changes in investment levels and offers an allowed
62 ROE in the 11.10% to 11.50% range.² Or they could invest in an Alabama gas utility
63 with an allowed return above 13% that has gas-cost pass-through and an annual
64 adjustment for changes in projected usage per customer, O&M expenses, depreciation,
65 other taxes, and investment levels.³ The Division and Committee may rationalize their
66 unreasonably low recommendations by comparing them to those few gas utilities with
67 allowed returns in the 9% range. The Commission needs to consider where rational
68 investors would be more likely to invest their capital. No matter how well reasoned a
69 Commission order is, adopting the Division's or Committee's recommendation will
70 damage Questar Gas' ability to provide adequate, reliable utility service. Division
71 witness Peterson acknowledges that "[t]he recommended cost of equity may be perceived
72 by Wall Street as too low relative to Questar Gas peers." (Direct Testimony of Charles E.
73 Peterson (Peterson) at lines 144-145.)

74 Later he stated,

75 Part of Bluefield and Hope criteria is the ability to attract capital. At this
76 time, I know of no evidence that Wall Street (i.e. the financial markets)
77 would be expecting cost of equity awards in the low 9% range. An award
78 of 9.25% by the Commission might have ramifications for the Company's
79 bond rating and otherwise its ability to attract capital. (Peterson at 1005-
80 1008.)

81 These statements should be enough for the Commission to reject the Division and
82 Committee recommendations. I urge the Commission to consider carefully Division
83 witness Peterson's own concerns as well as the above questions in rejecting the Division
84 and Committee recommendations.

¹ Final Decision, Docket No. 5-UR-103 (Wis. PSC, Jan. 17, 2008)..

² Decision 07-12-049, Applications 07-05-003, et al., (Cal. PUC, Dec. 21, 2007) at 56.

³ Letter from Alagasco to Alabama Public Service Commission re Dockets 18046 and 18328 (Feb. 29, 2008).

85 **Q. Would Commission adoption of the Division and Committee allowed ROE**
86 **recommendations negatively impact Questar Gas credit ratings?**

87 A. Very likely. The recent Moody's Questar Credit Opinion included the following
88 statements regarding the Questar Gas A3 rating:

89 [Questar] Gas faces near-term regulatory risk with the rate case filed in
90 January 2008, with a decision expected by early fall of 2008. The rating is
91 based on a constructive outcome with allowed returns within range of
92 industry means. The company is stabilized from weather normalization
93 (though at the customer option) and a decoupling mechanism, which was
94 recently extended through 2009.

95 [Questar] Gas' stable outlook incorporates some potential weakening in
96 free cash flow and debt metrics as it implements a multi-year feeder line
97 replacement program. [Questar] Gas faces near-term regulatory risk with
98 a rate case that it recently filed with new rates expected in the fall of this
99 year. An unfavorable outcome with allowed returns below industry norms
100 could pressure the ratings.

101 Both the Division and Committee recommended allowed ROEs are "below industry
102 norms" as shown in Mr. Hevert's Chart 1. They are at or below the bottom of the range
103 of recently allowed ROEs. A Commission decision at this level would result in weaker
104 credit metrics and would likely put downward pressure on Questar Gas' credit ratings.
105 This would have a direct impact on the ability of Questar Gas to raise capital and the cost
106 of that capital.

107 **Q. Have you had personal experience in raising capital for Questar Gas?**

108 A. Yes. I have sat across the table from both debt and equity investors. I know they require
109 competitive returns. I know the returns they are able to get on their investments in other
110 gas utilities with similar risks. The allowed ROE recommended by Mr. Hevert will allow
111 Questar Gas to compete for capital. The allowed returns recommended by the Division
112 and Committee will not.

113 **Q. Would a Commission decision approving the Division's or Committee's**
114 **recommendation threaten Questar Gas' ability to provide adequate, safe and**
115 **reliable utility service to its customers?**

116 A. Yes. The bottom line is this—continued growth in the number of customers, an aging
117 distribution system, and growing peak-day demand will require continued new capital to
118 maintain, replace, expand, and upgrade high-pressure feeder lines, main lines and service
119 lines. Adoption of the Division’s or the Committee’s recommended allowed ROE would
120 weaken our ability to attract the investment dollars necessary to connect new customers.
121 It would weaken our ability to attract the investment dollars necessary to replace our
122 aging feeder line system.

123 **Q. What is your conclusion?**

124 A. I urge the Commission to reject the Division and Committee recommendations and adopt
125 the allowed ROE recommended by Mr. Hevert.

State of Utah)
) ss.
County of Salt Lake)

I, Alan K. Allred, being first duly sworn on oath, state that the answers in the foregoing written testimony are true and correct to the best of my knowledge, information and belief. Except as stated in the testimony, the exhibits attached to the testimony were prepared by me or under my direction and supervision, and they are true and correct to the best of my knowledge, information and belief. Any exhibits not prepared by me or under my direction and supervision are true and correct copies of the documents they purport to be.

Alan K. Allred

SUBSCRIBED AND SWORN TO this 28th day of April, 2008.

Notary Public