BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

IN THE MATTER OF THE JOINT NOTICE AND APPLICATION OF QUESTAR GAS COMPANY AND DOMINION RESOURCES, INC. OF PROPOSED MERGER OF QUESTAR CORPORATION AND DOMINION RESOURCES, INC.	))))))))))	**DOCKET NO. 16-057-01** **DPU Exhibit 1.0 DIR** **Direct Testimony** **Douglas D. Wheelwright**

FOR THE DIVISION OF PUBLIC UTILITIES
DEPARTMENT OF COMMERCE
STATE OF UTAH

Direct Testimony of

Douglas D. Wheelwright

July 7, 2016

I. INTRODUCTION AND SUMMARY

Q: Please state your name, business address and title.

A: My name is Douglas D. Wheelwright; my business address is 160 East 300 South, Salt Lake City, Utah 84114. I am a Technical Consultant with the Division of Public Utilities (Division).

Q: On whose behalf are you testifying?

A: The Division.

Q: Please describe your position and duties with the Division.

A: As a technical consultant, I examine public utility financial data and review filings for compliance with existing programs as well as applications for rate increases. I research, analyze, document, and establish regulatory positions on a variety of regulatory matters. I review operations reports and evaluate the compliance with the laws and regulations. I provide written and sworn testimony in hearings before the Utah Public Service Commission (Commission) and assist in the case preparation and analysis of testimony.

Q: Please summarize your educational and professional experience.

A: I hold a Bachelor's degree in Finance from Weber State University. Prior to working for the Division, I was a financial advisor for 10 years and held SEC Series 7, 9, 10, 63, and 66 licenses. I began working for the Division in 2008 and have attended the NARUC Advanced Studies Program at Michigan State University and have completed a number of other utility regulation training courses. I have earned the professional designation Certified Rate of Return Analyst (CRRA) from the Society of Utility and Regulatory Financial Analysts. I have provided testimony to the Commission and appeared as a Division witness in a number of previous Questar Gas and PacifiCorp dockets.

II. OVERVIEW

Q: What is the purpose of your testimony in this matter?

A: I will provide comments on the proposed merger and will introduce the other Division witnesses. I will not attempt to discuss all of the individual details of the merger transaction but I will address specific issues and concerns within the filing. Other Division witnesses will address the individual items and commitments contained in the merger agreement as well as ring fencing guidelines.

Q: Please identify the Division's witnesses for this docket.

A: The Division is sponsoring three witnesses: Mr. Charles Peterson, Ms. Kathleen Kelley, and me. Mr. Peterson is employed by the Division and will present information concerning ring fencing concerns and guidelines that should be considered with this merger. As part of the review process, the Division has hired outside consultants from Daymark Energy Advisors, Inc. (Daymark), formerly known as LaCapra Associates, to evaluate the general merger commitments. Specifically, Daymark evaluates whether the commitments meet the Commission standard requirement to demonstrate a net benefit to ratepayers.[1] Ms. Kelly from Daymark will provide testimony and analysis on behalf of the Division.

Q: Please summarize the Division's position and conclusions concerning the proposed merger of Dominion Resources, Inc. (Dominion) and Questar Corporation (Questar, Questar Corp., or the Corporation).

A: The Division believes that Dominion and Questar have the burden of proof to demonstrate that the proposed merger resulting in Dominion Questar Gas (DQG) will result in a net benefit to Utah ratepayers. Based on the information that has been filed and after review of the numerous data request responses, the Division does not believe that there are quantifiable benefits that would support approval of the merger. While Dominion and Questar have identified a few general benefits, there are many unanswered questions related to corporate overhead charges, financing of the operating entities and ring fencing protections that could far exceed any identified benefits. Without additional information and commitments from Dominion and Questar, the Division is unable to determine a net benefit and recommends

[1] Docket No. 05-035-54, MidAmerican Energy Holdings and PacifiCorp, January 27, 2006 (Subsequent History Omitted) and Docket No. 98-2035-04, ScottishPower/PacifiCorp Merger, November 23, 1999.

that the Commission reject the proposed merger. If the Commission were to approve the proposed merger, there would need to be additional commitments and assurances from Dominion. The position of the Division is incorporated in the testimony of the three Division witnesses with specific ring fencing guidelines and recommendations included in DPU Exhibit 2.3 attached to Mr. Peterson's direct testimony.

Q: Please briefly summarize the work and investigations that has been performed in this case.

A: The Division has reviewed the testimony of Questar and Dominion witnesses along with the attachments and exhibits. The Division and its consultants have submitted 205 data requests to the Company and have reviewed additional data responses from other intervening parties in both Utah and Wyoming[2].

Q: Will you briefly summarize the current structure of Questar Corporation and explain why it is important to understand the relationship of these entities in understanding the proposed merger?

A: Yes. Questar Corporation (Questar Corp, or the Corporation) is a holding company with three principal complementary lines of business. Each of the operating entities is a wholly owned subsidiary with 100% of the stock of the operating company owned by Questar Corp. The fourth business unit (Questar Fueling) has only six employees[3] and separate financial information is not available.

1. **Questar Gas Company (Questar Gas)** distributes natural gas as a public utility in Utah, Southwest Wyoming and small portion of Southwest Idaho. Questar Gas had 990,381 customers as of year-end 2015 with 97% of the customers located in Utah. Sales to residential and commercial customers are seasonal. The typical residential customer consumes 80% of their annual gas usage during the coldest six months of the year. Questar Gas has a number of approved programs to reduce the volatility of the

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[2] Questar filed Docket Nos 30010-150-GA-16 and 3025-1-GA-16 with the Wyoming Public Service Commission.
[3] DPU Data request 1.09

customer's bills and to reduce the volatility of Questar Gas' gross margin.[4] Questar Gas has 930 employees or approximately 53% of the total employees in the Questar Corp. workforce.

2. **Wexpro** develops, produces and delivers natural gas from cost-of-service reserves for Questar Gas under the terms of the Wexpro I and Wexpro II Agreements. By agreement, Wexpro can supply up to 65% of the forecast annual gas requirement of Questar Gas.[5] Wexpro has 143 employees or approximately 8% of the total workforce. Approximately 95% of Wexpro's total revenue comes directly from Questar Gas.
3. **Questar Pipeline** provides natural gas transportation and underground storage services in Utah, Wyoming and Colorado. Pipeline companies' rates and charges for storage and transportation of natural gas in interstate commerce are regulated by the FERC. Questar Pipeline has 269 employees or approximately 15% of the total workforce. Approximately 28% of Questar Pipeline's total revenue comes directly from Questar Gas.
4. **Questar Fueling and Questar Corporation**. Questar Fueling builds, owns and operates compressed natural gas (CNG) fueling stations for fleet operators for medium and heavy duty trucks and tractors. Financial results from this entity are not separately reported and are not material to the consolidated operations.

   Questar Corp. includes the shared services for accounting, compliance, legal, audit, human resources, information technology, purchasing, communications and insurance services for all of the subsidiary companies. Questar Corp and Fueling have 417 employees or approximately 24% of the total workforce. Questar Corp. does not generate income but does assign direct and indirect costs to each company for shared services.

The three primary operating entities provide the total revenue and net profit for the corporation. Each of the operating entities also pay regular dividends to the holding company and provide the source of funds for Questar Corp to pay dividends to its

[4] E.g. Weather Normalization, Conservation Enabling Tariff (CET) and Demand Side Management (DSM).
[5] Docket 13-057-13, Settlement Stipulation, page 4, paragraph 12a.

shareholders. It is important to understand the interconnection of the operating entities to the total corporation and how allocated costs of each of the operating entities may ultimately be passed on to the regulated customers of Questar Gas.

Q: Why do you believe it is important to understand Questar Corporation before even discussing the detail of the proposed merger of Questar Corporation and Dominion?

A: As part of the analysis of the proposed merger, it is important to understand what shared services costs from Questar Corp may be reduced and what additional corporate costs may be allocated by Dominion. As will be shown later, an understanding of corporate cost allocation must be obtained in order to determine if the proposed merger will result in a net benefit to ratepayers.

Q: Can you summarize the annual net income information from the operating entities?

A: Yes. Historical balance sheet, income statement and cash flow summaries have been included for Questar Corp., Questar Gas, Wexpro and Questar Pipeline as DPU Exhibit 1.1 – 1.4. Information in the Questar 10-K filing indicates that Questar Fueling was not profitable as of year-end 2015 and has relatively small asset base. No financial information for Questar Fueling has been included and is not included separately in the 10-K reporting. The summary information in Table 1 below has been taken from Questar's SEC 10-K filing and clearly shows the contribution of each of the operating entities to the total net profit of the corporation.

Table 1

Questar Corporation - Net Income and Loss by Lines of Business

(Dollars in Millions)	2011	2012	2013	2014	2015	5 Yr Avg %
Questar Gas	46.1	47.1	52.8	55.2	64.3	26%
Wexpro	95.2	103.9	110.6	122.8	98.9	52%
Questar Pipeline	67.9	64.7	8.2	60.6	59.6	26%
Corporate and Other	(1.3)	(3.7)	(10.4)	(12.1)	(14.1)	-4%
Net Income	207.9	212.0	161.2	226.5	208.7	

In summary, Wexpro has provided 52% of the net income for the Corporation over the past five years and remains very important to Questar Corporation. Questar Gas and Questar Pipeline have each provided 26% of the net income over the past five years.

Q: Has Questar Corporation indicated that it is concerned about the continuation of future earnings from Wexpro?

A: Yes. The 2015 10-K report provides insight into the future earnings concern.

> Wexpro's earnings growth depends on its ability to develop gas reserves that are economically recoverable. Productive natural gas and oil reservoirs are generally characterized by declining production rates that vary depending on reservoir characteristics. Because of significant production decline rates in several of Wexpro's production areas, substantial capital expenditures are required to develop gas reserves to replace those depleted by production. [6]

In 2015, the Public Service Commissions in Utah and Wyoming approved modifications to the Wexpro agreements to lower the allowed rate of return for new development drilling along with several other changes. The lower return would affect only new wells completed after 2016. Existing wells would not be impacted and would continue to earn the higher rate of return. While the lower rate of return may allow some future drilling, the current market conditions and extended low price of natural gas may limit future developments. In the 2015 SEC 10-K report, Questar acknowledged that "the Company expects Wexpro's overall earnings to decrease compared to prior years." [7] Since Wexpro has historically produced over 50% of the net income, a decrease in earnings would have an impact on the net income for Questar Corporation.

Q: Do each of the operating entities pay dividends to the Questar Corporation?

A: Yes. Each operating entity is a separate corporation with regular dividend payments to the parent company. Below is a summary of the dividend history from the operating entities for the past five years. The dividend payments from the operating entities remained stable from 2012 through 2014 but Wexpro's increased dramatically in 2015.

[6] Questar Corporation 2015 10-K, page 17.
[7] Questar Corporation 2015 10-K, page 17.

Table 2

Dividends paid[8]

(Dollars in Millions)	2011	2012	2013	2014	2015
Questar Gas	30.3	33.0	35.5	36.0	38.0
Wexpro	59.4	64.0	67.5	68.0	180.0
Questar Pipeline	30.9	63.0	64.0	64.0	64.0
Dividends to Questar Corp	120.6	160.0	167.0	168.0	282.0
Questar Corp Dividend	110.1	117.4	124.6	131.9	148.0

With the sustained low price of natural gas, Wexpro has slowed the drilling program and reduced its capital expenditures. This condition caused an excess cash position and Wexpro paid $180 million in dividends to the Corporation in 2015.

Q: Do each of the operating entities have the same capital structure as the total Corporation?

A: No. The capital structure of each entity is unique. Wexpro has no long term debt and is 100% equity financed compared to Questar Gas with 53% equity and Questar Pipeline with 56% equity. Table 3 below provides a summary of the five year average long-term debt and equity positions for each of the operating entities and for the total corporation.

Table 3

5 Year Average Long Term Debt and Equity

	Questar Gas	Wexpro	Questar Pipeline	Questar Corp
LT Debt	46.8%	0.0%	44.3%	51.2%
Equity	53.2%	100.0%	55.7%	48.8%

Questar Corp. has a lower equity percentage than the individual operating entities. The lower equity position of the total Corporation is due to additional long-term debt and the pension liabilities that are held at the corporate level and are not allocated to the individual operating entities.[9]

Q: Do you have a concern with the different capital structures?

[8] DPU Data Request 2.11.
[9] DPU DR 1.07.

A: My concern is that the additional debt and liabilities can be unrecognized at the operating company level. The holding company has no ability to generate revenue or retire the debt and the pension liabilities are due to employees at each of the operating entities. With lower equity at the parent company level, the same earnings from the operating entities calculates to a higher return on equity at the corporate level. Let me illustrate this using a page from the Questar Corp. investor presentation for year-end 2015.

Table 4

FY 2015 Adjusted Return on Equity[10]

	Questar Gas	Wexpro	Questar Pipeline	Questar Corp
Return on Equity	10.5%	15.2%	10.8%	17.6%

With additional debt and liabilities held at the corporate level, the operating entities show higher equity levels which result in lower calculated return on equity. If the corporate debt and the additional liabilities were to be imputed or allocated to each of the operating entities, the calculated ROE may be greater than the Commission allowed return. This is one of the challenges with the holding company having greater leverage than the individual operating companies. A copy of the referenced page from the investor presentation has been included as DPU Exhibit 1.5.

Q: Why do you believe it is important to understand the capital structure and earnings of each of the operating entities?

A: Dominion is proposing to purchase all of the operating entities under the Questar Corp. umbrella. Wexpro and Questar Pipeline derive a large portion of their revenue from direct sales to Questar Gas. Goods and services from the affiliated companies as well as a large portion of the allocations of corporate overhead is ultimately paid by Questar Gas ratepayers. An understanding of the interconnection of these operating entities is critical to understanding what restrictions may need to be put in place in order to protect Questar Gas ratepayers from potential unintended consequences of the proposed merger.

[10] Questar Corporation – Fourth Quarter 2015 Earnings Release, February 18, 2016, page 14.

III. MERGER OVERVIEW

Q: Has Dominion indicated the main purpose for the merger of Questar and Dominion?

A: Yes. Mr. Farrell stated that "Dominion intends the Merger to be about growth, rather than cost reduction and plans to utilize Dominion Questar as its Western regional hub to supply the expanding needs for both gas and electric energy infrastructure in the western United States."[11] From this statement and others in the application, it appears that this merger is an opportunity for Dominion to expand its corporate footprint in the west and to look for further business opportunities.

Q: Does the filing indicate an estimated time frame for full integration of Questar into the Dominion operation?

A: No. Responses to data requests indicate that it will take some time to convert various Questar functions to those used by Dominion. It is estimated that converting some of the existing systems may not be completed until the end of 2017.[12] Maintaining duplicate systems along with integration costs from both Questar and Dominion could potentially add to the total overhead cost paid by Utah ratepayers. Without an understanding of which of the existing costs will be eliminated and which costs may increase, it is difficult to determine or calculate a net benefit. The application states that "Dominion Questar Gas will reflect any resulting benefits to customers in its future general rate cases".[13] There has been no information concerning how potential cost savings or increased costs will be calculated, reported, or monitored.

Q: The application indicates that Questar Gas will be left to operate as it does today. Do you believe that this is the case?

A: Somewhat. It appears that Dominion will allow the Questar operating entities to function similar to the way they have operated in the past; however, there will likely be a few changes

[11] Thomas F. Farrell II, page 4, line 95.
[12] OCS Data request 2.23.
[13] Application, page 12, paragraph 31.

for Questar Gas and for Questar Pipeline. In response to DPU Data request 3.03 Dominion stated the following:

> The proposed merger will result in a combined organization that will benefit from enhanced financial scale and access to capital, additional expertise and insight on operations and growth strategies especially in gas distribution, transmission and storage, and a broader and more national perspective on key industry issues and trends. As a result, Questar and its operating subsidiaries stand to benefit in their ability to identify, evaluate, compete for, invest in, and successfully operate growth investments that add to Questar's existing ability to serve customers and communities and facilitate regional growth.[14]

This statement indicates that DQG would not be left to operate as it has in the past but will be looking for new opportunities as directed by Dominion.

Q: The application indicates that Dominion will provide up to $75 million in additional funding for the defined benefit plan. Have you been able to determine if the additional contribution would benefit Questar Gas ratepayers?

A: No. In response to DPU data request 3.04 and 3.05, Questar estimated that if the full $75 million were contributed it could reduce the pension cost allocated to Questar Gas by $2.7 million in the first year. The calculation includes a number of assumptions and there has been no reconciliation to determine the primary reason for the unfunded pension amount. The defined benefit plan is maintained at the corporate level and is not allocated to the operating entities. Without a reconciliation of previous contribution amounts from the operating entities, the Division is unable to determine if the amount allocated to Questar Gas is appropriate. In addition, the Dominion commitment identifies "up to $75 million" and is based on market conditions at some point in the future. Thus in reality, the actual amount that will be contributed has not been determined and the corresponding benefit, if any, cannot be determined.

[14] Response to DPU Data Request 3.03.

IV. CORPORATE COST ALLOCATION

Q: Can you summarize the amount of corporate cost that has been allocated from Questar and the way that these costs are allocated to the operating entities?

A: Yes. Questar uses both direct and indirect allocation to assign corporate overhead cost to the operating entities. DPU Exhibit 1.6 provides additional detail concerning the direct and indirect amounts and the percentage of corporate costs that have been paid by the operating units over the last 5 years. Table 5 below is a summary of the total amount of corporate overhead that has been paid by the operating entities.

Table 5

Questar Corporation - Charges Allocated to Operating Entities[15]

(Dollars in Millions)	2011	2012	2013	2014	2015	5 Yr Avg
Questar Gas	81.3	30.4	38.9	17.8	65.0	46.7
Wexpro	11.6	78.2	54.0	90.9	89.7	64.9
Questar Pipeline	39.1	25.7	44.3	53.1	60.5	44.5
Questar Fueling		0.0	-2.2	-3.1	1.3	(1.0)
Total Corporate Charges	131.9	134.2	134.9	158.7	216.5	155.2

The total dollar amount of the corporate cost has averaged $155.2 million per year for the past five years. Corporate cost allocation is very important since a large portion of the costs allocated to the affiliated companies will indirectly be paid by the ratepayers of Questar Gas.

SEC 10-K information indicates that 95 – 97% of the revenue for Wexpro is paid by Questar Gas and approximately 28% of the revenue for Questar Pipeline comes from Questar Gas. Accordingly, virtually all of the corporate costs allocated to Questar Gas and to Wexpro are currently paid by Questar Gas ratepayers as well as 28% of the corporate cost allocated to Questar Pipeline. Based on historical averages, I have calculated that approximately 80% of all the corporate cost has been paid by the ratepayers of Questar Gas either directly or indirectly. That amount is estimated to be $171.9 million in 2015 and averages $124.0 million per year for the last five years.[16]

[15] DPU data request 2.05 and 5.01.
[16] DPU Exhibit 1.6.

It is unclear how much of the corporate cost could be reduced or reallocated to Dominion if the merger is completed. It is also unclear how much additional corporate cost will be allocated to the Questar operating entities from Dominion. Since corporate cost allocation to the affiliated companies is passed through to Questar Gas customers, the Commission may want to look at possible limits on the total dollar amount that could be allocated to all of the Questar affiliated companies and not just Questar Gas. As part of the request for approval, Dominion should have identified and included specific dollar limits on the amount of total corporate overhead that would be allocated to DQG in future years.

Q: Do you have any information on how the direct and indirect corporate cost has been allocated specifically to Questar Gas?

A: Yes. As mentioned, a more complete look at the cost allocation has been included in DPU Exhibit 1.6. Indirect costs are allocated based on a Distrigas formula that is based on a number of allocations factors such as the gross plant, gross revenue less product cost, and gross payroll.[17] Direct costs are allocated to the operating unit if there is a direct tie to the service that is performed such as legal or accounting services. As shown in the table below, the majority of the volatility in the dollar amount of overhead that has been allocated to Questar Gas has been due to the wide fluctuation in direct charges. A summary of the total direct and indirect charges allocated to Questar Gas are as follows:

Table 6

Questar Corporation - Charges Allocated to Questar Gas[18]

(Dollars in Millions)	2011	2012	2013	2014	2015	5 Yr Avg
Direct	49.5	(3.5)	3.8	(16.9)	29.4	12.4
Allocated Charges	31.8	33.9	35.1	34.8	35.6	34.2
Total	81.3	30.4	38.9	17.8	65.0	46.7

The table indicates that the allocated charges under the Distrigas formula are fairly consistent from year to year. Direct charges to Questar Gas have varied dramatically from year to year primarily due to tax allocations. As mentioned, the merger application does not indicate how

[17] DPU data request 2.07.
[18] DPU data request 2.05 and 5.01.

much of the existing Questar corporate overhead could be reduced or eliminated due to the proposed merger.

Q: Does the application indicate the amount of corporate costs from Dominion that may be allocated to Questar Gas in the future?

A: No. The application does not address the amount of corporate overhead that will be allocated to any of the operating entities. In response to DPU data request 4.01, Dominion stated;

> It is anticipated that Dominion shared services will perform some of the same services that are performed currently by Questar Corporation. The corporate support functions are currently working together towards a plan for integration. At this point in the process, projected costs for the integrated Company going forward have not been quantified.

In the initial application, Dominion stated that the combination of shared services "may result in lower costs to Dominion Questar Gas for these services over time."[19] There is no commitment or assurance that costs would be lower under the Dominion ownership - only that costs "may" be lower.

Q: Have you been able to determine the amount of corporate cost that has been allocated to any of the existing Dominion affiliated companies?

A: Yes. Dominion has referenced its Dominion East Ohio, which is a natural gas distribution company and is comparable in customer size to Questar Gas. In response to DPU data request 10.2, Dominion provided the direct and indirect cost that had been billed to Dominion East Ohio for the past five years. It is unclear if the corporate allocation to Questar Gas will be similar to Dominion East Ohio but a review of the historical information does provide a point of reference for comparison purposes.

[19] Application, page 12, paragraph 31.

TABLE 7

Dominion Resources Services, Inc. (DRS) - Billing to Dominion East Ohio[20]

(Dollars in Millions)	2011	2012	2013	2014	2015	5 Yr Avg
Direct	28.0	33.7	32.2	25.5	25.6	29.0
Indirect	25.3	25.0	26.3	25.8	24.5	25.4
Total	53.3	58.7	58.6	51.3	50.1	54.4

The corporate cost allocation to Dominion East Ohio appears to be more consistent than the Questar Corp allocation to Questar Gas, however the five year average allocation of $54.4 million is higher than the $46.7 million historical average paid by Questar Gas.

Dominion has not provided an estimate of the corporate cost that would be allocated to any of the Questar affiliated companies. With approximately 80% of all corporate cost that may be allocated to Questar Gas, Wexpro, and Questar Pipeline ultimately being paid by Questar Gas ratepayers, there must be a clear understanding of the corporate cost allocation not only to Questar Gas but also to all of the affiliated companies. Based on the current information that is available, it appears that the corporate allocation cost for Questar Gas could potentially be higher if the merger were to be approved. Once again, no net benefit to Utah ratepayers is apparent.

V. CAPITAL STRUCTURE

Q: Do you agree with the representation that Dominion has a 61% debt and 39% equity position as filed in the application? [21]

A: No. The calculation used in the application follows Dominion's revolving credit covenant calculation that is different than regular accounting methods.[22] Following the calculation method used in GAAP accounting, Dominion would have 66% debt 34% equity as of year-end 2015. From a long-term perspective, Dominion has remained fairly consistent with an average of 64% debt and 36% equity for the past five years. The Division has included DPU

[20] DPU data request 10.2.
[21] Application, page 8, paragraph 20.
[22] Response to DPU Data Request 1.06.

Exhibit 1.7 which is a summary of the Dominion Resources financial information from SEC 10-K filings for the past five years.

Q: Do you agree with the representation that Questar Corporation has a 42% debt and 58% equity position as filed in the application? [23]

A: No. The calculation used in the application did not include $250 million in current maturities of long term debt that was scheduled to be refinanced just prior to the announced merger. The current maturity amount was refinanced with short-term debt but should be included in the long-term debt calculations. The refinance was delayed due to the pending merger but remains as a long-term obligation. Questar also had unusually high short-term debt as of year-end 2015, a portion of which will be refinanced into additional long-term debt. Excluding the long-term debt artificially increases the equity percentage. Questar Corp. has maintained a fairly consistent capital structure of 51% debt and 49% equity for the past five years. If a merger of the two companies were to be approved, the Division would recommend that DQG rates be set based on a capital structure that is similar to the historical average.

Q: Are you concerned with the lower equity position of Dominion compared to Questar Corporation?

A: Yes. My concern goes back to the same issue mentioned above where Questar Corp. currently has a lower equity position than its operating entities. Dominion has a 36% equity position compared to Questar's 49% equity. This lower equity and greater levels of debt create greater financial risk since future earnings are needed to pay interest and to ultimately repay the debt. Additional debt can also impact a company's credit rating and borrowing cost, as will be discussed by Ms. Kelly of Daymark. Additional debt can also be a concern should interest rates increase in future years adding to the total interest expense and reducing net income.

[23] Application, page 7, paragraph 16.

VI. FINANCING

Q: Has Dominion indicated how the merger with Questar will be financed?

A: Yes. The merger will be financed with a combination of debt and equity financing. In the April 28, 2016 technical conference, Dominion indicated that 67% of the purchase will be financed with equity and equity linked securities and the remaining 33% would be financed with long term debt.

The 67% equity portion of the transaction is identified in three parts: Mandatory Convertible Notes $1.25 billion, Dominion Equity $0.50 billion and Master Limited Partnership (MLP) Drop Proceeds $1.20 billion. While Dominion has classified all three as equity transactions, they should not be considered as equity as of the initial purchase date. As of the closing date, the only equity funding will be the Dominion stock which represents 11.4% of the purchase. The remaining 88.6% will be debt financing.

Q: Can you discuss the MLP Drop portion of the equity funding?

A: Yes. Dominion has identified the MLP Drop proceeds as the portion of the Questar Pipeline assets that will be transferred to the Master Limited Partnership. Dominion has indicated that this portion of the transaction will take approximately one year and represents 27.3% of the proposed equity. With the addition of the MLP proceeds and the initial Dominion equity, one year after the initial purchase, the equity portion of the transaction will have increased to 38.6% with 61.4% remaining as debt financing.

Q: Can you discuss the mandatory convertible debt offering that is proposed to finance a portion of the Questar purchase?

A: Yes. The proposed instruments have not been marketed or priced so the specific terms are unknown at this time; however, mandatory convertible instruments have been used by Dominion in the past. In response to DPU data request 7.04, Dominion indicated;

> The current base assumption is that the company will again use the same structure for this financing as has been utilized in the past. Under this framework, the equity conversion is expected to occur three years after the issuance of the original units.

The conversion to equity for this portion of the financing does not occur until three years after issuance and represents 28.4% of the proposed equity. All parties and the Commission should understand that the total 67% equity position in the purchase transaction is not achieved until three years after closing and is based on a number of assumptions about what will occur over that time frame.

Q: Can you summarize how Questar Gas is currently financed and has Dominion indicated how the ongoing operations of DQG will be financed?

A: Yes. Questar Gas currently has an intercompany lending agreement that has been in place since 1984 to manage short term borrowing needs. The current program allows Questar to manage cash at the corporate level and the individual operating companies are allowed to borrow and lend to the parent company at favorable interest rates. Long term debt funding is issued by Questar Gas.

Under the proposed merger agreement, DQG would issue its own commercial paper to finance short term borrowing needs. In response to data requests, Dominion and Questar have provided historical interest rates for short term borrowing. The Division has reviewed the information and found that short term interest rates for both Dominion East Ohio and Dominion Resources are higher than the short term interest rate for Questar Gas. Over the past 16 months the short-term rate for Questar Gas was 0.39% compared to 0.58% for Dominion East Ohio and Dominion Resources.[24] With projected higher cost for short-term borrowing, it is difficult to demonstrate that the proposed merger will result in a net benefit to Utah ratepayers. The proposed lending structure will eliminate the current inter-company lending agreement within the Questar Corp.

Q: Has Dominion explained how Wexpro will be financed?

A: No. Dominion has not indicated how Wexpro will be financed, which could be a concern since Wexpro plays an integral role in Questar Gas' operation. It appears likely that Wexpro will participate in the Dominion money pool for financing, similar to the way that Dominion

[24] DPU Data request 7.01, 7.02 and 7.03.

East Ohio and the other Dominion companies are financed. This type of financing may not create the necessary ring fence protection for Wexpro.

Q: Are you concerned about this type of financing for Wexpro?

A: Yes for two reasons. First, as identified previously in my testimony, the short-term borrowing rate at Dominion is higher than the current inter-company borrowing rate at Questar. Second, without sufficient ring fencing protections, Wexpro could potentially be subject to the negative intra-affiliate issues and market or other influences on the parent company.

Q: Do you have any other concerns about the continuing operations of Wexpro?

A: Yes. There appears to be some confusion concerning the eligibility of Wexpro assets in future MLP offerings. It is the Division's understanding that Wexpro assets were to be excluded from any future MLP offerings, however, the June 2016 Dominion investor presentation show both Questar Pipeline and Wexpro as MLP eligible.[25] This issue should be explained and clarified for all parties.

Q: Do you have any information from parties in Wyoming concerning the Dominion Questar merger?

A: Yes. On July 1, 2016, Denise Kay Parrish filed testimony with the Wyoming Public Service Commission on behalf of the Office of Consumer Advocate with the following recommendation. "The OCA recommended that the Joint Application be denied unless and until there is agreement upon or the Commission directs additional conditions and projections."[26]

[25] Dominion Investor Presentation, June 2016, page 19.
[26] Docket Nos. 30010-150-GA-16 and 30025-1-GA-16, Direct Testimony of Denise Kay Parrish, page 9, line 30.

VII. CONCLUSIONS AND RECOMMENDATIONS

Q: What conclusions have you reached concerning the proposed merger of Dominion Resources and Questar Corporation?

A: Based on previous Commission decisions, in order for a proposed merger to be approved, the parties must demonstrate that the transaction will result in a net benefit to ratepayers and that the transaction will result in just and reasonable rates. In the Division's view, Dominion and Questar have not demonstrated that there are quantifiable benefits that would support approval of the merger. The Division has identified many unanswered questions related to corporate overhead charges, financing of the operating entities and ring fencing protections, which have not been addressed and could impact ratepayers. Without additional information and commitments from Dominion and Questar, the Division is unable to determine a net benefit and would recommend that the Commission reject the proposed merger. If the Commission decides to approve the merger, additional commitments and assurances must be put in place to protect Questar Gas and its ratepayers. Specific guidelines and recommendations for ring fencing have been included in the testimony of Ms. Kelly and Mr. Peterson. The Division adopts and supports the recommendations included in the testimony and as summarized in DPU Exhibit 2.3.

Q: Does this conclude your testimony?

A: Yes.