

TABLE OF CONTENTS

I. Introduction.....	4
II. Summary of Conclusions	7
III. Overview of the Proposed Transaction.....	9
IV. The Utah Standard for Acquisition of Public Utilities.....	15
V. Company Size vs. Access to Capital Markets	16
VI. Ring Fencing Provisions to Protect Ratepayers.....	23
VII. Review of Proposed Merger Transaction and Transition Costs	36
VIII. Merger Savings Credit	50
IX. What Concerns Should the Commission Have Regarding the Proposed Transaction?	59
X. Utah Ratepayer Protections.....	62
XI. Conclusion	64

ATTACHMENTS

DPU Exhibit 3.1 DIR, Resume of Kathleen Kelly

DPU Exhibit 3.2 DIR, Commitments Made by Joint Applicants

DPU Exhibit 3.3 DIR, Ring Fencing Provisions

DPU Exhibit 3.4 DIR, Additional Merger Conditions

1 **I. Introduction**

2 **Q. What is your name and business address?**

3 A. My name is Kathleen Kelly. I am employed by Daymark Energy Advisors, Inc.
4 (“Daymark”) as a Managing Principal Consultant. My business address is One
5 Washington Mall, Boston, MA 02108.

6
7 **Q. On whose behalf are you testifying in this proceeding?**

8 A. I am submitting testimony on behalf of the Utah Division of Public Utilities (“Division”
9 or “Staff”) with regard to the Application filed on March 3, 2016 (the “Application” or
10 the “Filing”) by Dominion Resources, Inc. (“Dominion”) and Questar Corporation
11 (“Questar”) (“Joint Applicants”) with the Utah Public Service Commission (the
12 “Commission” or “PSC”) for approval of the acquisition of Questar by Dominion
13 (“Merger” or “Acquisition”). Questar Gas Company (“Questar Gas”) is a subsidiary of
14 Questar, and serves as a local natural gas distribution company (“LDC”) in Utah, Idaho,
15 and Wyoming. This matter has been designated as Docket No. 16-057-01.

16

17 **Q. Please describe your education and employment background.**

18 A. I received my MBA from Northeastern University and a BS degree in Mathematics from
19 the University of Massachusetts. Since joining Daymark in February of 2016, I have
20 worked on projects related to mergers and acquisitions, investments in energy
21 infrastructure, energy markets, and regulatory rate cases. Prior to joining Daymark, I
22 worked at Lummus Consultants International, Inc. which was formerly known as Stone &
23 Webster Management Consultants, leading a practice in utility management and

24 planning. In this role I advised utilities, developers, large customer groups, and
25 regulators with regard to utility planning, management and operations, in particular with
26 regard to evaluating acquisitions, business operational efficiencies, and business and
27 regulatory strategy. Throughout my career, I have gained and demonstrated considerable
28 experience and expertise in many utility-related matters. My resume is provided as DPU
29 Exhibit 3.1 DIR.

30

31 **Q. Please summarize Daymark and its business.**

32 A. Daymark Energy Advisors is the new name of the firm formerly known as La Capra
33 Associates. The name change occurred on November 9, 2015. Daymark provides
34 consulting services in energy planning, market analysis, and regulatory policy in the
35 electricity and natural gas industries. We serve a national and international clientele from
36 our offices in Boston, Massachusetts and Portland, Maine providing consulting services
37 to a broad range of organizations involved with energy markets, including renewable
38 energy producers, private and public utilities, transmission owners, energy producers and
39 traders, energy consumers and consumer advocates, regulatory agencies, and public
40 policy and energy research organizations. Our technical skills include power market
41 forecasting models and methods, economics, management, planning, rates and pricing,
42 energy procurement and contracting, and reliability assessments. Our experience
43 includes detailed analyses of energy and environmental performance of the electric
44 systems, economic planning for transmission and distribution, and market analytics.

45 **Q. Have you previously testified before the Commission?**

46 A. No.

47

48 **Q. What is the purpose of your testimony in this proceeding?**

49 A. The purpose of my testimony is to address the following issues:

- 50 • Whether the acquisition complies with the Utah standard for holding company
51 acquisitions.
- 52 • Whether there are financial risks to Questar if the acquisition is approved.
- 53 • If the acquisition occurs, whether the operations of Questar may be negatively
54 impacted.
- 55 • If the acquisition occurs as proposed, evaluate the risks and benefits to Questar Gas
56 ratepayers and Utah citizens.
- 57 • Whether there are appropriate ring fencing provisions to protect Questar from
58 affiliate-related impacts.
- 59 • Whether there are adequate benefits to support the acquisition.
- 60 • If the acquisition is to be approved, identifying conditions to approval that should be
61 established to protect customers of Questar Gas and Utah citizens.
- 62 • To propose conditions and to make recommendations on behalf of the Division
63 concerning the above if the Merger is to be approved.

64

65 **Q. What exhibits are you sponsoring?**

66 A. In addition to this direct testimony and my resume, I am sponsoring three Exhibits:

- 67 • DPU Exhibit 3.2 DIR summarizes the commitments already made by the Joint
68 Applicants relative to Merger implications;
- 69 • DPU Exhibit 3.3 DIR provides ring fencing conditions which I submit that the
70 Commission should adopt if the proposed Merger is approved;
- 71 • DPU Exhibit 3.4 DIR provides additional conditions relative to reporting
72 requirements, service quality, capital investment, and organizational management that
73 I submit should be adopted by the Commission if the Merger is approved to ensure
74 that Questar Gas ratepayers are not harmed by the Merger.
- 75

76 **II. Summary of Conclusions**

77 **Q. Please summarize your conclusions and recommendations regarding the issues**
78 **addressed in your testimony.**

79 A. Based upon my review, I offer the following conclusions:

- 80 • The Filing cites a number of benefits, one of which is that as one of the largest
81 energy infrastructure participants in public equity and debt capital market, the
82 combined company will benefit from an enhanced ability to finance system
83 growth. However, no evidence has been provided by Dominion or Questar to
84 show that a larger company will actually have such improved access relative to
85 Questar today. To the contrary, Daymark has performed an independent
86 assessment which shows that larger companies do not necessarily result in
87 improved access to capital markets.

- 88 • Neither Dominion nor Questar has provided adequate evidence of any
89 quantifiable benefits to Questar Gas ratepayers or Utah citizens and in fact have
90 stated repeatedly that Questar will continue the majority of its current
91 management and operational policies and commitments.
- 92 • Due to the lack of concrete information in order to analyze and evaluate its
93 implications, potential exists for the acquisition to cause harm to Quester Gas
94 ratepayers.
- 95 • The commitments identified in the application in this proceeding (“the
96 Application”) are inadequate to (1) protect Questar Gas ratepayers from potential
97 harm and (2) to provide any quantifiable benefit, and thus will require additional
98 ring fencing and operational conditions to protect Questar Gas ratepayers and
99 Utah citizens.

100 Based upon these conclusions, I find that because there are no identified Merger benefits
101 that will accrue to Questar Gas ratepayers and Utah citizens, the proposed Merger is not
102 in the public interest, and this Merger, as proposed, does not meet the standard for the
103 Commission approving Dominion’s proposed acquisition of Questar Corporation.

104 Therefore, the Merger as proposed should not be approved. However, if the Commission
105 should approve the proposed Merger, Daymark emphatically suggests the Commission
106 impose additional conditions – as described in this testimony – in order to adequately
107 protect Questar Gas ratepayers and Utah citizens.

108

109 **Q. Has the Commission imposed conditions on prior merger approvals in Utah?**

110 A. Yes, the Commission has conditionally approved mergers in Docket No. 98-2035-04
111 relative to the ScottishPower PacifiCorp merger in 1999; in Docket No. 84-057-10
112 relative to the creation of Questar Holding Company by Mountain Fuel; and in Docket
113 No. 05-035-54 relative to the acquisition by MidAmerican Energy Holdings of
114 PacifiCorp.
115

116 **III. Overview of the Proposed Transaction**

117 **Q. Please briefly describe the proposed transaction.**

118 A. Dominion proposes to acquire all of the outstanding common stock of Questar
119 Corporation. Each existing share of Questar Corporation stock will be exchanged for
120 \$25.00 in cash. The transaction was announced on February 1, 2016.
121

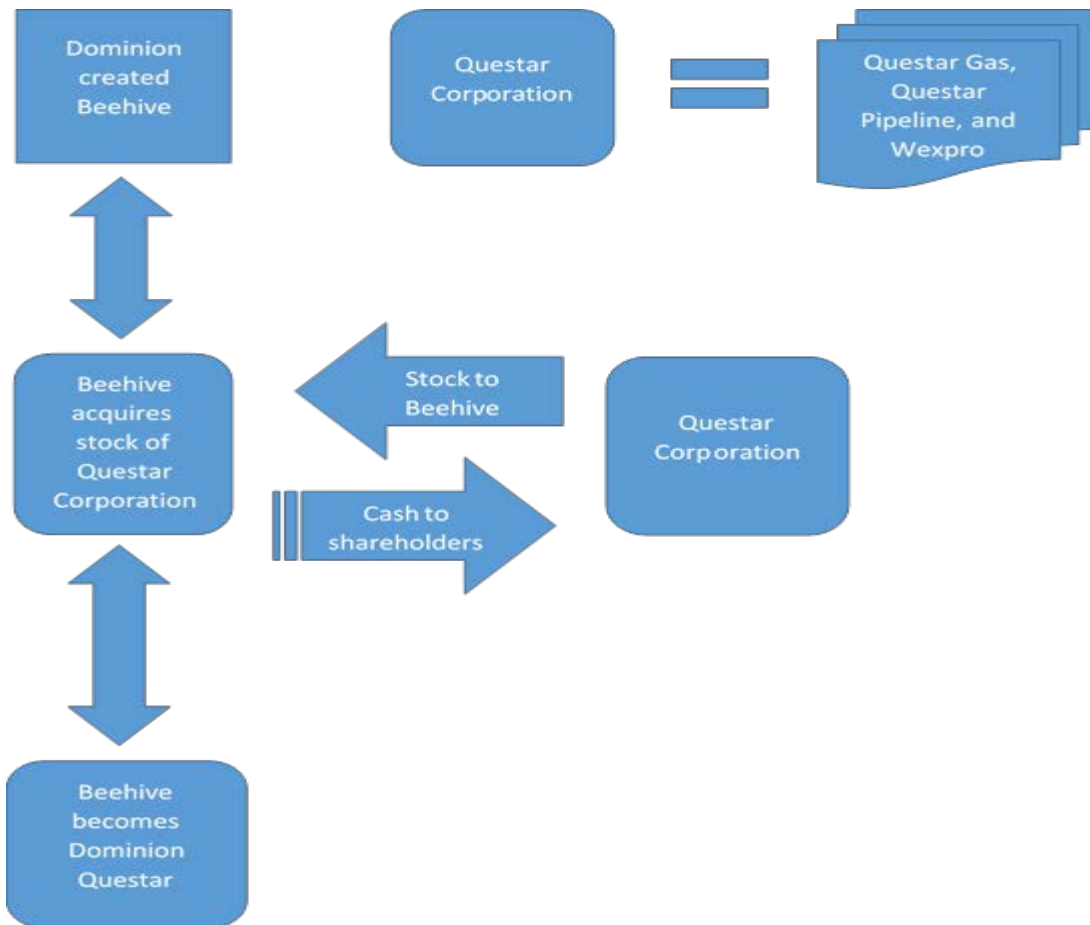
122 **Q. How is the transaction structured?**

123 A. According to the Joint Application, Dominion has created an acquisition entity known as
124 Diamond Beehive Corp (“Beehive”) for the purpose of acquiring the stock of Questar
125 Corp., in exchange for cash.¹ Shares of Questar Corp. will be exchanged for cash with
126 Beehive, and the shares of Beehive will be converted to common shares of Dominion
127 Questar.² While the transaction is described in more detail in the Merger agreement
128 itself,³ the overall structure of the transaction can be represented as follows:

¹ Joint Application of Questar Gas Company and Dominion Resources, Inc. of Proposed Merger of Questar Corporation and Dominion Resources, Inc., 2016, p. 3. (“Joint Application”).

² *Id.*, pp. 5-6.

³ *Id.*, Exhibit 1.1.



129

130 **Q. Are there any other parts of the proposed new business arrangement that you found**
131 **important?**

132 A. Yes. At some point after the Merger, Dominion “expects to contribute all or part of
133 Questar Pipeline to Dominion Midstream Partners, LLP, a Master Limited Partnership
134 (“MLP”).⁴ According to the Joint Application, “Dominion Midstream is a master limited
135 partnership formed by Dominion in 2014. Dominion Midstream invests in a growing
136 portfolio of natural gas terminaling, processing, storage, transportation, and related

⁴ Id., p. 10.

137 assets. Dominion owns 100 percent of the general partner and 64.1 percent of the limited
138 partner interests in Dominion Midstream.”⁵

139

140 **Q. What is the approximate value of this transaction?**

141 A. According to Questar’s (QTR)⁶ 2015 SEC Form 10K report, QTR had about 175 million
142 shares of common stock outstanding. The closing stock prices for Dominion (DOM) and
143 QTR just prior to the merger announcement were \$72.17 and \$20.39 per share
144 respectively. The total value of cash consideration to be paid by DOM for each QTR
145 share is about \$4.38 billion.⁷ Thus, DOM is paying about \$806 million or an 18.4%
146 market premium to acquire QTR.⁸

147

148 **Q. What is the stated purpose of the proposed transaction?**

149 A. According to the Application, the transaction is in the best interests of utility consumers,
150 investors, and the public because it will:⁹

- 151 • create a larger and financially stronger utility company with improved access to
152 capital markets;¹⁰
- 153 • strengthen each of the Utah operating companies by integrating best practices in
154 areas such as distribution operations, large capital project management, gas
155 supply, system reliability and customer service;¹¹

⁵ *Id.*, Footnote 2.

⁶ Questar’s stock ticker symbol is STR.

⁷ 175 million QTR shares multiplied by \$25.00 per share.

⁸ 175 Million QTR shares multiplied by \$20.39 per share.

⁹ Joint Application, pp. 24-32.

¹⁰ *Id.*, p. 31, Paragraph 59(j).

¹¹ *Id.*, p. 31, Paragraph 59(i).

- 156 • the Joint Applicants’ rationale for the proposed Merger is premised on the ability
157 to grow Dominion’s and Questar’s regulated infrastructure profile and is not
158 focused on achieving cost reductions;¹²
- 159 • maintain Questar’s tradition of making significant contributions to regional
160 economic development and generous support of educational, cultural, and
161 charitable activities in the communities they serve;¹³
- 162 • create a more diversified portfolio with a larger geographic footprint and provide
163 a base for Dominion’s anticipated West coast operations;¹⁴
- 164 • facilitate continued prudent investment in needed utility infrastructure, including
165 the ability to use the strong cash flow of the combined companies to fund future
166 investments without issuing new equity;¹⁵ and
- 167 • position the combined entity for continued growth.¹⁶

168

169 **Q. According to the Joint Applicants, what will be the benefits of this Merger for**
170 **Questar Gas ratepayers and citizens of Utah?**

171 A. As summarized in the testimony of Craig Wagstaff, President of Questar Gas Company,
172 in the Application, the benefits of this Merger include the following:

¹² *Id.*, p. 24, Paragraph 58.

¹³ *Id.*, p. 29, Paragraph 58(cc).

¹⁴ *Id.*, p. 24, Paragraph 58.

¹⁵ *Id.*, pp. 30-31, Paragraph 59.

¹⁶ *Id.*, p. 24, Paragraph 58.

- 173 • Questar Gas will continue to operate in a safe and reliable manner essentially as it
174 does today, and Dominion will provide additional benefits and strengths to all
175 stakeholders;¹⁷
- 176 • There will be potential benefits in the areas of customer service, safety,
177 community involvement, economic development, energy diversity and
178 geographical diversity through the sharing of best practices that will strengthen
179 the entire organization;¹⁸
- 180 • Dominion intends to increase historic levels of corporate contributions to charities
181 identified by local leadership that are within Questar Gas Company’s current
182 regulated retail operating areas by \$1,000,000 per year for at least five years and
183 to maintain or increase historic levels of community involvement, low income
184 funding and economic development efforts;¹⁹
- 185 • Dominion intends to establish a new Western Region Operating Headquarters in
186 Salt Lake City, Utah;²⁰
- 187 • Dominion intends to establish a newly formed advisory board for its western
188 operations composed of regional-based business and community leaders and one
189 of the discussion points of this board will be economic development activities;²¹
190 and

¹⁷ Wagstaff, p. 2, lines 37-39.

¹⁸ *Id.*, p. 4, lines 81-82.

¹⁹ *Id.*, p. 5, lines 98-102.

²⁰ *Id.*, p. 5, lines 107-108.

²¹ *Id.*, p. 5, lines 107-109.

191 • A diverse energy portfolio such as is provided by this Merger can strengthen a
192 company financially, the geographical diversity of Dominion allows resources to
193 be deployed to help Questar Gas manage customer inquiries, communication, and
194 service restoration.²²

195

196 **Q. Have the Joint Applicants quantified any of these claimed benefits?**

197 A. No. The Joint Applicants have repeatedly indicated in the Application filed with the
198 Commission, the Joint Applicants' presentations at the April 28th and 29th technical
199 conferences in Utah and Wyoming respectively, and the Joint Applicants' responses to
200 numerous requests for information, that there is no formal quantitative analysis of the
201 savings. However, as stated by Mr. Wagstaff in his testimony:

202 While it is ultimately the decision of the Board of Directors to determine whether
203 a proposal is in the best interest of the shareholders of the Company, the executive
204 management team was fully involved in analyzing and evaluating the impact of
205 the Merger on customers, employees and other stakeholders. I provided
206 information and feedback to the Board of Directors as they made their decision.
207 The executive management team considered the impact that the Merger would
208 have on the customers, employees of the Company, and the communities in which
209 we serve.²³

210 The investigation into the benefits of the proposed Merger has produced little evidence
211 that a quantitative benefits analysis of the proposed Merger was conducted. Testimony
212 provided by Mr. John Reed on behalf of Wisconsin Energy Corporation in Docket No.
213 14-0496 relative to a request for Merger Approval²⁴ states that typical merger savings can

²² *Id.*, p. 6, lines 118-119, 124-126.

²³ *Id.*, p. 2, lines 29-35.

²⁴ Testimony of John Reed, CEO Concentric Energy Advisors, Joint Application Exhibit 3.0 page 34 lines 712-715, Docket 14-0496.

214 range from 3% to 5% of non-fuel Operating and Maintenance Costs (“O&M”), these are
215 cited as net of initial investment to achieve the savings, or net benefits.

216 Without evidence of such net benefits, the primary justification for the transaction
217 appears to be the creation of a bigger company that Dominion believes will have better
218 access to capital markets. No quantifiable benefits to Questar Gas ratepayers or Utah
219 citizens have been estimated, projected, or apparently considered when assessing the
220 impact of this Merger. Section V of this testimony provides specific information relative
221 to my review of benefits to Questar Gas ratepayers and citizens of Utah.

222

223 **Q. Have the Applicants offered any commitments for the post-Merger management**
224 **and operation of the organization?**

225 A. Yes. The Applicants have provided a number of statements relative to management,
226 financial, and operational approaches and objectives following the close of the Merger.
227 These are summarized in DPU Exhibit 3.2 DIR.

228

229 **Q. Are these commitments sufficient to protect the Questar Gas ratepayers and the**
230 **citizens of Utah?**

231 A. No. These commitments are in most cases good objectives but require more clarity and
232 specificity and should be conditions if the Merger is to be approved.

233

234 **IV. The Utah Standard for Acquisition of Public Utilities**

235 **Q. Are you an attorney?**

236 A. No. Therefore, I am not drawing legal conclusions.

237 **Q. What is the standard of approval set forth in the Application?**

238 A. According to the Application, the Utah statutes that may apply in determining whether
239 approval of the Merger is required under Utah law are Utah Code Ann. §§ 54-4-1, 54-4-
240 25, 54-4-28, 54-4-29, and 54-4-30. Because the ownership of the shares of Questar Gas
241 Company stock is transferring to Dominion from Questar, this triggers the applicability
242 of section 54-4-29.

243

244 **Q. How do you interpret this standard?**

245 A. The Utah Merger standard is that the proposed transaction must be in the public interest.
246 Daymark has supported the interpretation in other merger cases and here that, in order to
247 be in the public interest, the proposed transaction must produce net benefits. Simply
248 causing no harm while producing no benefits does not meet this public interest standard.
249 This is generally consistent with the Commission orders in the prior merger cases.

250

251 **V. Company Size vs. Access to Capital Markets**

252 **Q. Has Dominion provided any analysis that shows that a larger company has better**
253 **access to capital markets?**

254 A. No. Dominion has not provided any such analysis.

255

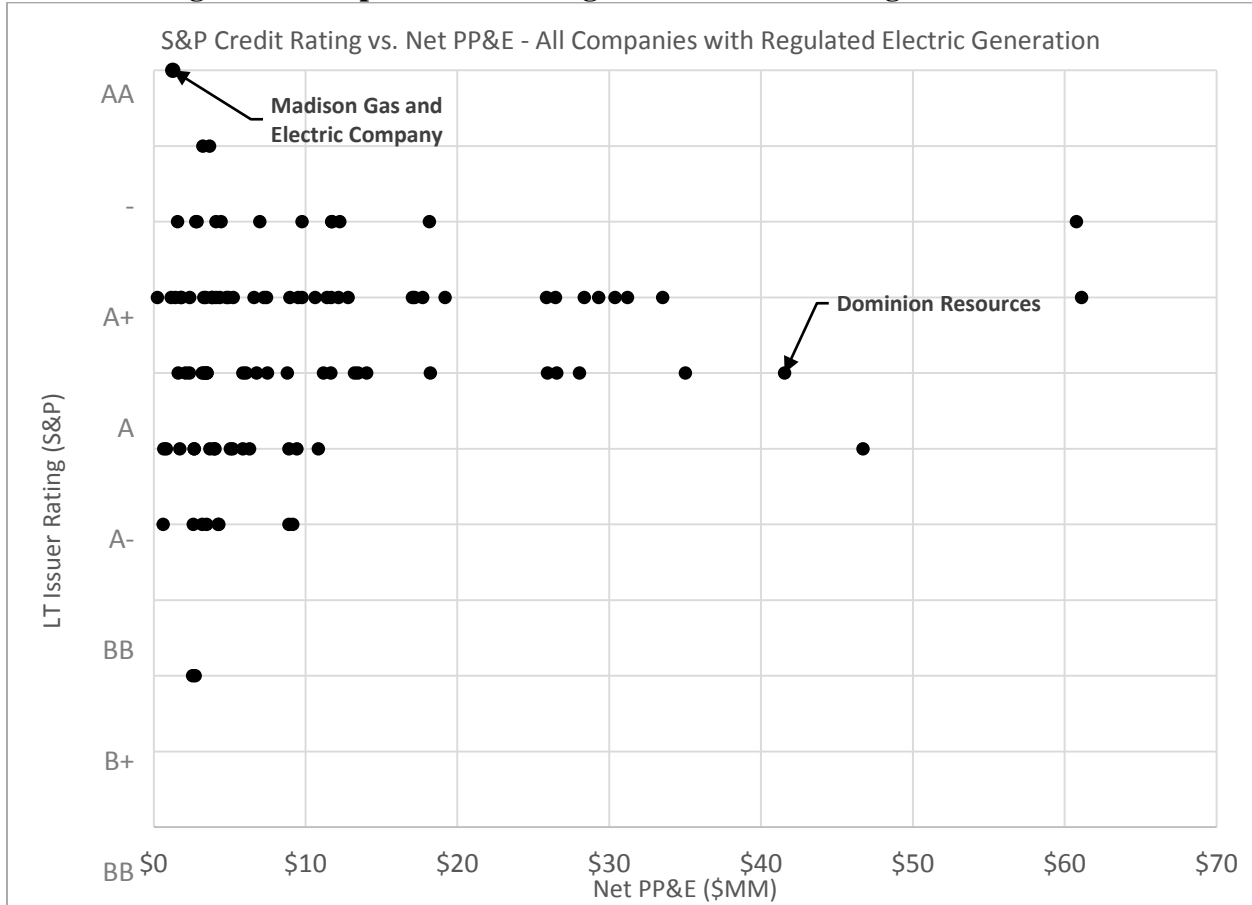
256 **Q. Were you able to analyze whether larger companies have greater access to capital**
257 **markets?**

258 A. Yes. The key factor influencing a company's ability to access capital markets is directly
259 related to that company's credit rating.²⁵ Higher credit ratings allow a company to more
260 easily borrow money at less expensive interest rates. I analyzed the credit ratings of both
261 electric and natural gas companies by company size. I compared the Standard & Poor's
262 ("S&P") Long Term Credit Rating of electric and natural gas companies to company Net
263 Property Plant and Equipment (Net PP&E) size information. The companies used in this
264 comparison are all regulated electric and gas companies from the SNL Financial
265 database. Figure 1 below provides a diagram of credit ratings relative to company size.
266 There is no correlation in this data showing that company size has any impact on
267 increasing a company's credit rating. To further illustrate this point one can look at the
268 company with the highest credit rating, Madison Gas and Electric Company, a company
269 that is much smaller than Dominion and about the same size as Questar Corporation.

²⁵ Standard and Poors (S&P) Global Ratings definitions taken from the website -
https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352.

270

Figure 1: Comparison of Rating Relative to Size – Regulated Electric



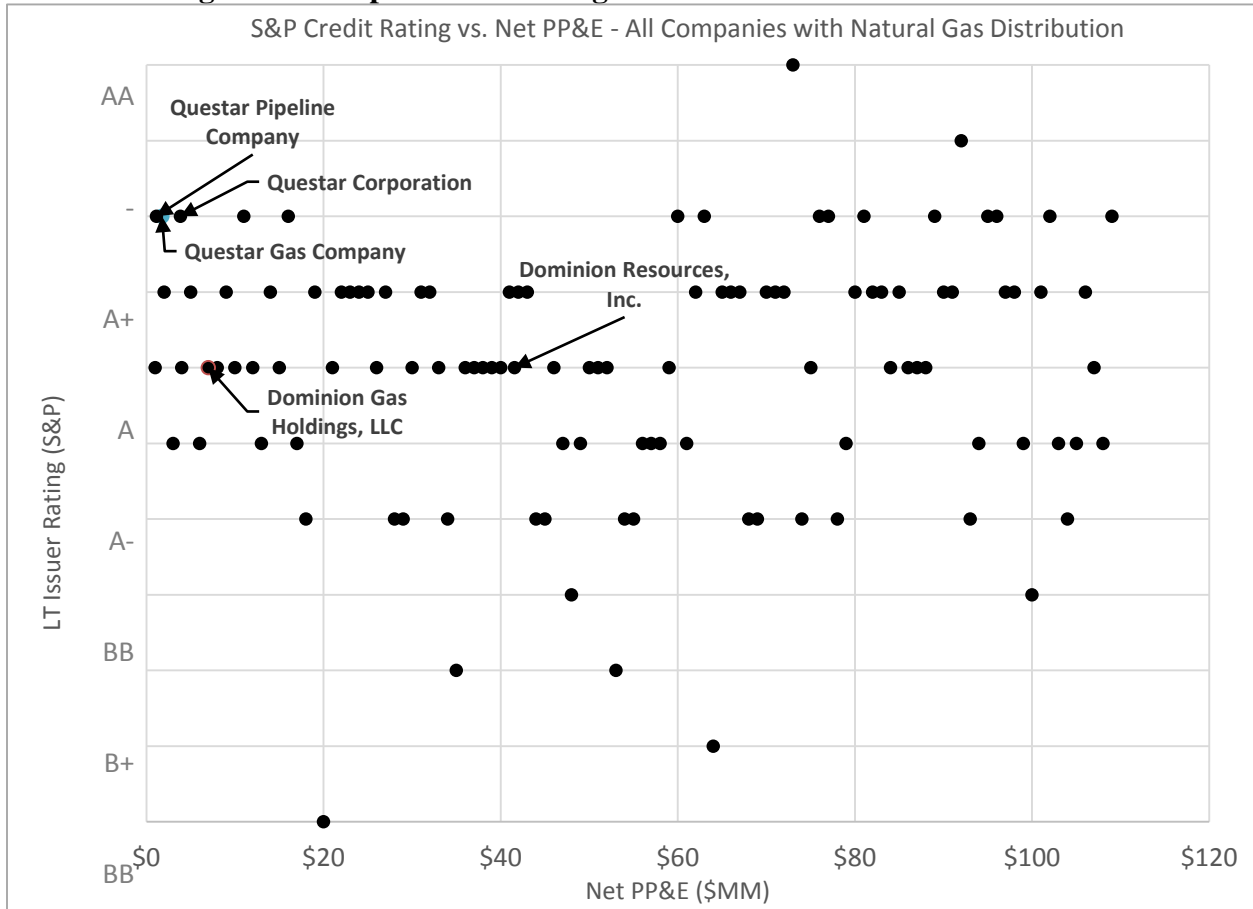
271

272 **Q. Were you able to make other, similar comparisons?**

273 A. I performed two other comparisons of company credit rating versus size. The first
274 includes companies with natural gas distribution and the second includes other parent
275 companies with regulated subsidiaries. Figures 2 and 3 below provide these
276 comparisons. These additional comparisons confirm the observation that there is no
277 apparent benefit to larger companies when it comes to obtaining a higher credit rating.

278

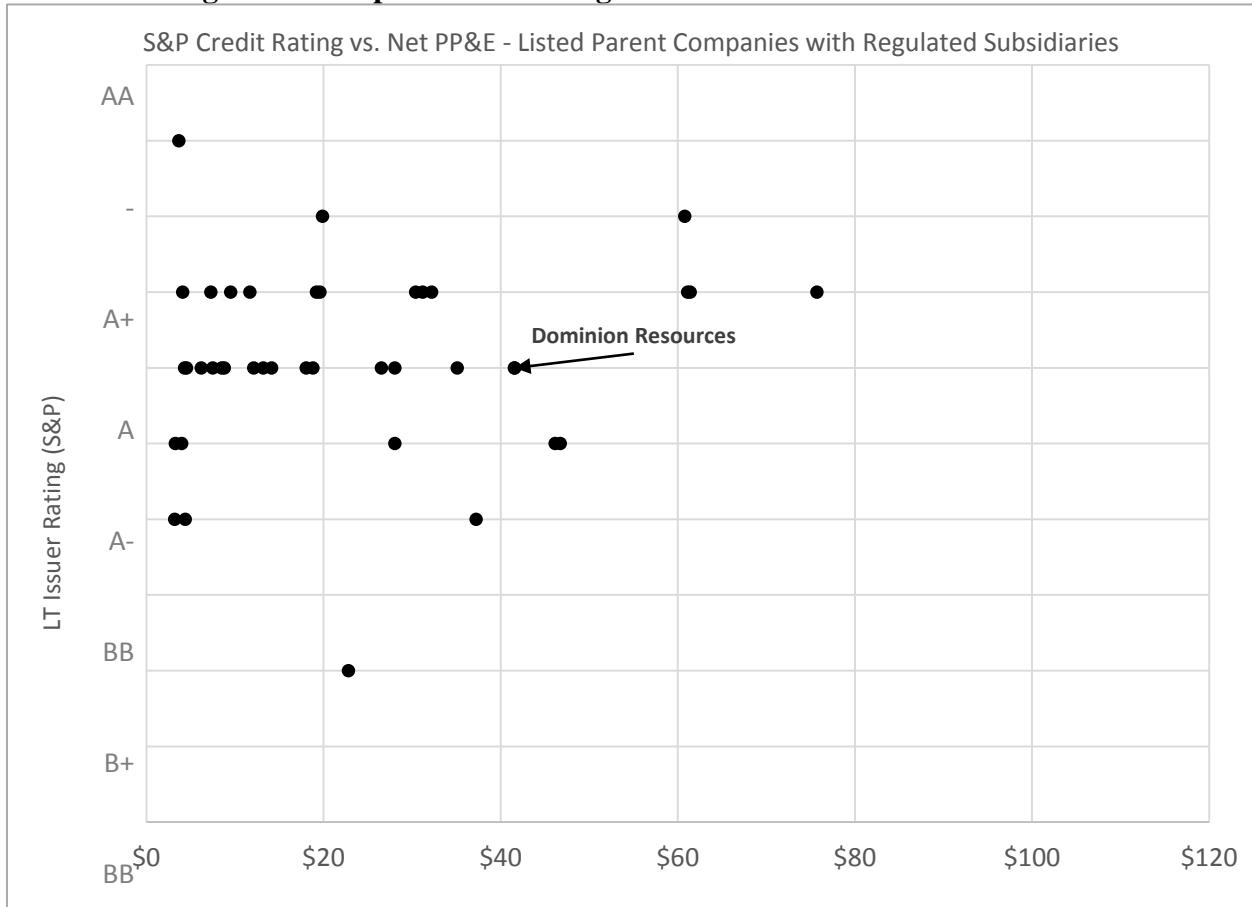
Figure 2: Comparison of Rating vs. Size – Natural Gas Distribution



279

280

Figure 3: Comparison of Rating vs. Size – Parent with Subsidiaries



281

282 **Q. Were you able to compare and evaluate the historic interest rates available to both**
 283 **Questar Gas and Dominion and its subsidiaries?**

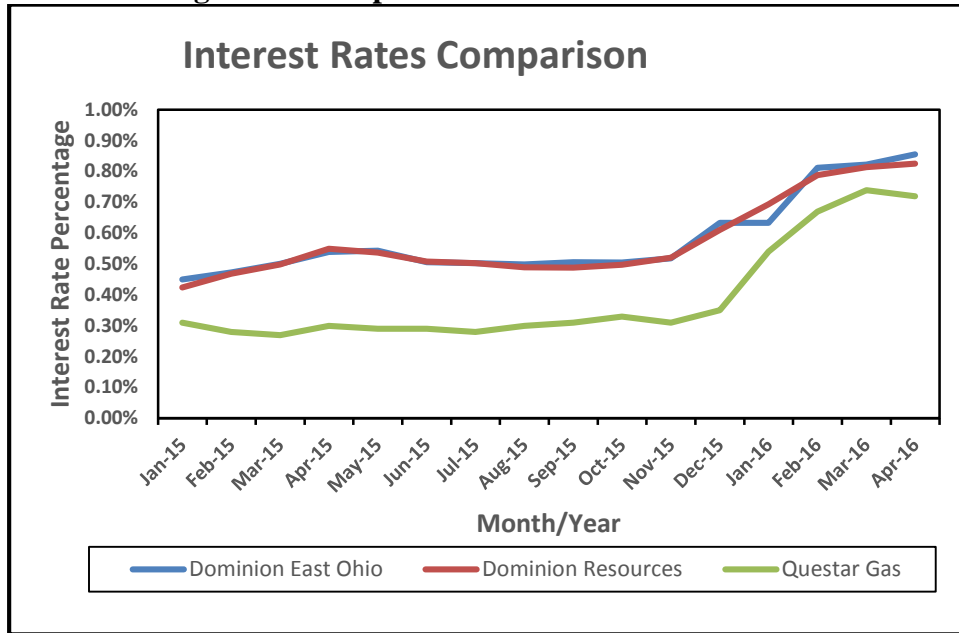
284 A. Yes. Figure 4 below provides a comparison over time of interest rates from Dominion
 285 East Ohio,²⁶ Dominion Resources, and Quester Gas.²⁷ The graph indicates that Dominion
 286 East Ohio paid nearly the same interest rate as Dominion Resources through
 287 intercompany lending. Questar Gas, on the other hand, had a noticeably lower interest
 288 rate over the same time period.

²⁶ Dominion East Ohio (“East Ohio Gas Company”) is a gas distribution company in Ohio owned by Dominion.

²⁷ Interest rate data provided in Joint Applicant’s responses to DPU 7.1, 7.2, and 7.3.

289

Figure 4 - Comparison of Recent Interest Rates



290

291 **Q. What do you conclude from this analysis?**

292 A. The Joint Applicants have provided no quantifiable analysis to support the assertion that
293 larger companies have improved access to capital markets and that the resulting Merger
294 will benefit Questar Gas ratepayers or citizens of Utah. The comparative analysis above
295 suggests no correlation between credit rating and company size. Coupling this assessment
296 with data provided by the Companies and compared in Figure 4, I conclude that there is
297 no evidence provided either by the Companies or that can be taken from our independent
298 analysis that there is a likely benefit for a larger company having improved access to
299 capital markets nor providing a benefit of such to ratepayers. In fact, Questar has enjoyed
300 lower rates than Dominion companies in the recent past.

301 **Q. Has the credit rating of either Dominion or Questar been affected by the Merger**
302 **announcement?**

303 A. Both have been impacted by the announcement of this Merger. S&P, on February 1st
304 2016, downgraded Dominion Resources to BBB+,²⁸ due to both the increased debt taken
305 on by this Merger and expectations that Dominion will “continue to pursue a growth
306 related acquisitions at a faster pace than peers”²⁹ suggesting it will likely continue to take
307 on increasing levels of debt. The nature of Dominion Resources Inc. with its Master
308 Limited Partnership, Dominion Midstream, creates incentive for the company to grow
309 through acquisitions. As suggested by S&P, “Questar Corp will be exposed to more risk
310 under the MLP of Dominion Resources”.³⁰ MLPs benefit from increased acquisitions as
311 they provide owners with tax deferred distributions (not considered dividends). MLPs
312 generally look to grow their distribution over time; as these distributions need to be
313 stable, predictable and substantive, third-party acquisitions tend to be a preferred method
314 for growing MLPs, implying Dominion will continue to grow at a substantive pace
315 through acquisitions as suggested by S&P and therefore continue to increase its debt
316 levels.³¹
317 Questar Corp was also placed on review for a downgrade from Moody’s on February 1st,
318 2016:

319 Moody’s underlines the fact that Questar Corp. is now held by a lower credit
320 quality entity which will control the strategic dividend and liquidity management
321 policies of Questar Corp. While the company has previously functioned as an
322 integrated entity between subsidiaries, legal and organizational divisions could
323 result in a divergence of this integrated strategic management... The intent to
324 transfer Questar Pipeline to Dominion Midstream exposes Questar Corp. to a

²⁸ Dominion Resources Inc. And Subsidiaries Downgraded To 'BBB+' On Acquisition Of Questar Corp.; Outlook Stable; <https://www.dom.com/library/domcom/pdfs/investors/fixed-income/sp-dri.pdf>.

²⁹ *Ibid.*

³⁰ *Ibid.*

³¹ *Ibid.*

325 higher risk profile as an integrated and consolidated Questar will be separated into
326 different subsidiaries of a larger lower credit quality entity.³²

327 As mentioned, Moody's believes that Questar Corp., acting as an unregulated subsidiary
328 to Dominion Resources, has the potential to be impacted by Dominion Resources' lower
329 credit rating. The new corporate structure and strategy, especially in regards to moving
330 Questar Pipelines to Dominion Midstream, affects the lower risk level of a previously
331 integrated utility. These two announcements demonstrate the risk introduced to both
332 companies as a result of this Merger.

333

334 **Q. Has this affected the credit rating of Questar's regulated gas utilities?**

335 Not yet. However, the almost immediate downgrade of Dominion and potential
336 downgrade of Questar's credit ratings demonstrate the uncertainty and added risk the
337 parent companies are exposed to with this Merger. The downgrades at the parent level of
338 this corporation demonstrate that corporate re-organization and strategic changes can
339 increase risk and without the proper ring-fences in place credit and borrowing costs can
340 easily increase for subsidiaries, adding unnecessary costs to the consumer at the expense
341 of merger synergies or growth at the parent company.

342

343 **VI. Ring Fencing Provisions to Protect Ratepayers**

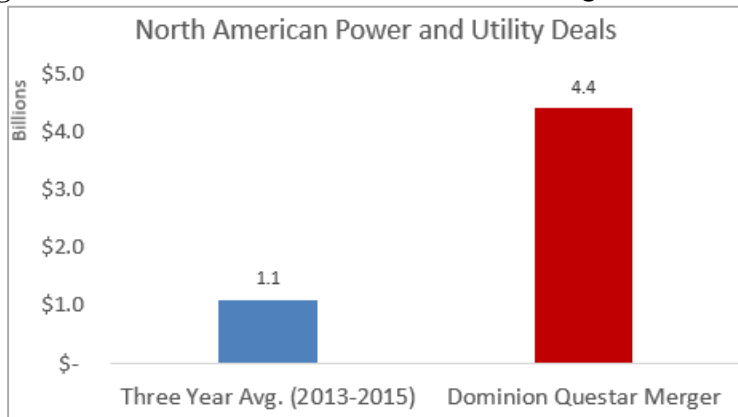
344 **Q. How is this merger different than the many utility mergers currently proposed or**
345 **recently approved?**

³² Moody's Places Questar Corp. on Review for Downgrade; Questar Gas and Questar Pipeline Affirmed; Outlooks Remain Stable - https://www.moodys.com/research/Moodys-Places-Questar-Corp-on-Review-for-Downgrade-Questar-Gas--PR_343115.

346 A. While utilities mergers have become common place in recent years, the proposed
347 Dominion Merger with Questar Corporation is unique and requires heightened due
348 diligence because of its size and complexity. The size and complexity are highlighted in
349 the following four key points:

350 1. The size and value of this merger dwarfs many recent utilities mergers at \$4.4 billion,
351 compared with the average utility deal over the last three years of \$1.1 Billion³³
352 (Figure 5).³⁴ This merger is four (4) times the size of the average utility deal. This
353 merger is also more than four (4) times the “mega deal” threshold established by
354 Price Waterhouse Cooper (PWC); classified as a utility deal above \$1 Billion.³⁵

355 **Figure 5 – PWC utilities deals vs. Dominion Questar Merger**



356
357 2. Questar is one of few truly vertically integrated gas utilities in North America,
358 Questar owns significant portions of the natural gas value chain in both Utah and
359 Wyoming. Questar’s direct subsidiary, WEXPRO, produces between 50% and 65%³⁶

³³ <http://www.pwc.com/us/en/power-and-utilities/publications/us-power-deals.html>.

³⁴ Data taken from PWC North American Power & Utilities Deals. <http://www.pwc.com/us/en/power-and-utilities/publications/us-power-deals.html>.

³⁵ *Ibid.*

³⁶ Trail Stipulation and Canyon Creek Stipulation – WEXPRO Agreements: <https://www.questargas.com/AboutUs/WEXDocs.php>.

360 of the gas consumed within Utah. Questar Pipeline, transports this gas to Questar Gas,
361 which then delivers the gas to 97% of the residential customers in Utah.³⁷ This
362 integrated nature requires close monitoring of the interaction between subsidiaries
363 and heightened regulatory oversight in order to prevent potential cross-subsidization
364 by Questar Gas ratepayers under a new corporate parent.

365 3. The varying degrees of regulated subsidiaries held by Questar Corporation, and to
366 whom these regulated entities are beholden add to the complexity of this Merger.
367 Questar Gas is regulated by utility commissions in Utah and Wyoming (its Idaho
368 portion is regulated through contracting with the neighboring states of Utah and
369 Wyoming to set rates and charges for customers in Idaho),³⁸ Questar Pipeline is
370 regulated by the Federal Energy and Regulatory Commission (“FERC”) and
371 WEXPRO produces cost of service gas through supervised arm’s length agreements
372 between Questar Gas and WEXPRO (supervised by the Utah and Wyoming
373 Commissions). The nature and scope of these regulations, and how these regulations
374 are enforced at the state versus the federal level makes the process of assessing and
375 monitoring the potential impact of this Merger to customers within these states
376 complex as well.

377 4. Whereas as Questar currently does not have a stake in power generation, Dominion
378 has a presence in the power market in Utah (through its existing solar project).³⁹

³⁷ <http://seekingalpha.com/article/3732056-questar-corp-working-together-create-value>.

³⁸ http://www.puc.idaho.gov/orders/recent/Order_No_33496.pdf.

³⁹ See Dominion Resources response to DPU 6.89.

379 Dominion views the Utah market as a potential area for growth⁴⁰ meaning the parent
380 company (Dominion Resources, Inc.) may have plans to add gas fired power
381 generation to the existing natural gas value chain in Utah; considerations must be
382 made in order to keep Questar's regulated utilities separate from Dominion's
383 developments in the power market, in order to protect consumers.

384

385 **Q. Is there potential for adverse outcomes and impacts to Questar's regulated gas**
386 **utilities?**

387 Without proper ring fencing requirements adopted by regulatory bodies, the failure of
388 non-regulated investments and strategies at the parent company level can expose the
389 regulated companies to increased risk.⁴¹ Without proper and substantive ring-fencing in
390 place, the unregulated parent company, can impact the financial stability and credit
391 ratings of its subsidiaries, and in the case of regulated utilities, impact the customer by
392 deferring risk and losses between its subsidiaries through various means. According to
393 Steven L. Schwarcz of Duke University, "...utility companies are ring-fenced to protect
394 them against internal and external risks, so they can be assured to be able to continue
395 providing the public with essential utilities such as power, clean water, and
396 communications".⁴² Examples of how this harm to regulated subsidiaries can occur are
397 outlined as follows:

⁴⁰ See Dominion Resources responses to DPU 3.03, DPU 6.89, OCS 2.36, and WSPC 1.06 Attachment 3 – Redacted Slide 4.

⁴¹ http://scholarship.law.duke.edu/cgi/viewcontent.cgi?article=5531&context=faculty_scholarship.

⁴² *Id.*, p. 105.

- 398 ○ Financial harm to subsidiaries can be incurred in the form of difficulty, or extra
399 expenses, in securing capital both efficiently and economically. This can occur if
400 changes in the parent’s credit rating company spread to its subsidiaries.
- 401 ○ Negative consequences to the utility’s operations due to a lack of insulation of the
402 regulated utility’s finances from the parent or other subsidiaries; e.g. requiring
403 financial transfers that allocate debt from unregulated to regulated subsidiaries or
404 requiring dividend payments from regulated subsidiaries.
- 405 ○ Declines in the overall service quality or reliability of the subsidiary. If there are
406 no safe-guards, a decline in service quality and reliability, resulting from a dictate
407 from the parent company through measures such as cost cutting, can impact the
408 overall risk profile of the regulated subsidiary.
- 409 ○ Limited access to information at the subsidiary level. Unless reporting
410 requirements are clearly defined, a commission may find that it does not have
411 access to sufficient, timely information to monitor conditions of the regulated
412 subsidiary, delaying Commission actions to prevent or address adverse effects
413 both financially and at the public safety level for customers.
- 414 ○ Cross-subsidization from the utility’s operations to non-utility affiliates by adding
415 extra costs to the utility’s customers for the benefit of the parent’s shareholders.
- 416 ○ Cross-subsidization from the utility’s operations to non-utility affiliates, adding
417 extra costs to the utility’s customers for the benefit of the parent’s shareholders.
- 418 ○ The burden of significant merger transaction costs on subsidiaries utility
419 operations.

420

421 **Q. If the proposed transaction is to be approved, how can the Commission protect Utah**
422 **ratepayers from adverse outcomes?**

423 Questar, if the Merger is approved, will be directed by a parent company that has
424 significantly more exposure to unregulated risk including unregulated power generation,
425 unregulated retail gas marketing, unregulated midstream operations (Blue Racer
426 Midstream), three nuclear plants, and LNG exports facility operations (Cove Point).⁴³

427 This has the potential to expose Questar's regulated entities and its customers to
428 increased risk both through expanding unregulated operations of the parent company and
429 a greater debt load by borne by the parent company. If this Merger is to be approved, the
430 Commission should incorporate conditions in order to mitigate this risk and debt burden
431 from being imposed on Dominion's regulated subsidiaries and ergo on to ratepayers of
432 Questar Gas.

433

434 To limit the impact on Questar Gas and its ratepayers the Commission should consider:
435 limitations on dividends (especially in the case of WEXPRO), maintenance of separate
436 debt and debt ratings for Questar Gas, minimum and maximum equity and debt ratios
437 (capital structures), and borrowing and lending restrictions.

438

⁴³ Dominion Company profile. <https://www.dom.com/corporate/about-us/company-profile>.

439 These limitations and restrictions can effectively create a ring-fence around regulated
440 subsidiaries in order to prevent adverse impacts from other subsidiaries and the parent
441 company on the regulated subsidiaries.

442
443 The Commission should also require timely and adequate information from Questar Gas.
444 Reliable and timely information and open access to information in readily accessible
445 format maintained within Utah for the Commission review with appropriate
446 confidentiality controls is necessary to protect Questar Gas customers.

447
448 The Commission should create these necessary ring fencing measures through mandatory
449 conditions imposed upon Dominion and Questar as requirements for approval of the
450 Merger.

451
452 **Q. If the proposed transaction is to be approved, what specific ring fencing provisions**
453 **would you recommend be established by the Commission?**

454 A. My full list of recommended ring fencing provisions is provided in DPU Exhibit 3.3 DIR,
455 with additional Merger conditions in DPU Exhibit 3.4 DIR. Proposed conditions creating
456 ring-fences between regulated subsidiaries and the parent company are also provided by
457 the Joint Applicants:

- 458 • As proposed by Dominion and Questar in their Filing seeking approval of the Merger
459 transaction, following the Merger, Dominion Questar Gas should be operated in the

- 460 same manner as it is operated today, including keeping Dominion Questar Gas’
461 headquarters in Salt Lake City, Utah.⁴⁴
- 462 • For regulatory purposes, Dominion Questar Gas’ accounting will continue to reflect
463 assets at historical costs, approved depreciation rates and deferred income taxes based
464 on original cost in accordance with the Uniform System of Accounts.⁴⁵
 - 465 • Dominion will not record any portion of the cost to acquire or any goodwill
466 associated with the transaction on Dominion Questar Gas’ books and Dominion is
467 planning to make the required accounting entries associated with the transaction on
468 that basis.⁴⁶
 - 469 • Dominion will maintain credit metrics supportive of strong investment grade credit
470 ratings for Dominion Questar Gas.⁴⁷
 - 471 • Dominion Questar Gas will not transfer material assets to, or assume liabilities of,
472 Dominion or any other subsidiary of Dominion without prior Commission approval.⁴⁸
 - 473 • Neither Dominion nor its other subsidiaries will, without prior Commission approval,
474 make loans to Dominion Questar Gas that bear interest at rates that are greater than (i)
475 rates being paid at the time of such loan by Dominion or such other subsidiary on its
476 own debt or (ii) rates available, at the time of such loan, on similar loans to Dominion
477 Questar Gas from the market.⁴⁹

⁴⁴ Joint Application, p. 25, Paragraph 58(a).

⁴⁵ *Id.*, p. 27, Paragraph 58(o).

⁴⁶ *Id.*, p. 28, Paragraph 58(u).

⁴⁷ *Id.*, p. 28, Paragraph 58(x).

⁴⁸ *Id.*, p. 29, Paragraph 58(aa).

⁴⁹ *Id.*, p. 28, Paragraph 58(y).

- 478 • Dominion Questar Gas will lend funds to Dominion only in accordance with the
479 current practice of Questar Gas, whereby it occasionally provides short-term funds to
480 Questar Corporation as seasonal working capital needs fluctuate.⁵⁰
- 481 • As part of this and future regulatory proceedings, Dominion Questar Gas will provide
482 information about Dominion or its other subsidiaries relevant to matters within the
483 Commission’s jurisdiction to the Commission not the Division, upon request of the
484 Commission or Division, respectively.⁵¹

485 I view these conditions, as well as all those relating to ring fencing in DPU Exhibit 3.3
486 DIR, as necessary to ensure separate debt, credit ratings, borrowing and lending
487 restrictions, and dividend restrictions. These do not penalize the merging companies or
488 discourage mergers, but protect regulated subsidiaries from the impacts of unregulated
489 parent companies, with the ultimate goal of holding Dominion Questar Gas’ ratepayers
490 harmless from increases in financing or other costs.

491

492 **Q. Are you aware of any other acquisitions and/or mergers where the lack of ring**
493 **fencing provisions became an issue for a regulated subsidiary?**

494 A. Yes. There are numerous examples where a lack of ring fencing provisions led to credit
495 downgrades at the parent company being reflected and borne or potentially reflected and
496 borne by its subsidiaries, I include some examples below.

497

⁵⁰ *Id.*, p. 29, Paragraph 58(z).

⁵¹ *Id.*, p. 27, Paragraph 58(m).

498 **Q. Has there been any recent situation in which a lack of ring fencing could cause**
499 **negative financial impacts to subsidiaries?**

500 A. As recently as last month the Fitch ratings company, in the case of Great Plains Energy's
501 ("GXP") proposed acquisition of Westar Energy and Kansas Gas and Electric Co.
502 ("KGE"),⁵² stated that it placed Westar and KGE on review for a downgrade and
503 mentioned that ring fencing between GXP and Westar/KGE will be a key criteria into
504 determining if they will downgrade Westar and KGE.

505 GXP's deleveraging plan as well as the level of integration and/or *ring fencing*
506 going-forward will become key criteria in assessing Westar's and KGE's credit
507 profiles after the acquisition is completed.⁵³

508

509 **Q. Do you have a recent example where ring fencing measures prevented negative**
510 **impacts to public utility?**

511 A. In the mid-2000s Constellation Energy ("Constellation"), an energy producing, trading
512 and distributing company, which also owned the regulated utility - Baltimore Gas and
513 Electric Company ("BGE"), was outperforming both the S&P 500 and the S&P 500
514 electric utilities index.⁵⁴ Much of this success was due to its high-risk high-reward
515 merchant power and trading businesses, Constellation's energy trading went from a
516 supporting function to its key growth strategy in 2007. However in 2008, the liquidity
517 crisis effecting the larger economy, led to a liquidity crisis at Constellation and caused
518 the stock price to decline 70% in the period of two (2) months.⁵⁵

⁵² <http://www.businesswire.com/news/home/20160601007005/en/Fitch-Places-Westar-Negative-Watch-Acquisition-Announcement>.

⁵³ *Id.*

⁵⁴ <http://www.slideshare.net/finance12/constellation-energy-2005-annual-report>.

⁵⁵ http://www.mit.edu/~jparsons/publications/Constellation_JEnergyMarkets.pdf.

519
520 The illiquidity and credit-rating downgrades⁵⁶ (caused by the collapse of the stock price,
521 among other things) led to obligations by counterparties for Constellation to post
522 additional collateral, meaning that Constellation faced bankruptcy. Constellation also had
523 insufficient ring fencing in regards to BGE and Constellation controlled a majority of the
524 board seats at BGE, in other words, a bankruptcy at Constellation would mean a
525 bankruptcy at BGE.⁵⁷

526
527 Constellation however avoided bankruptcy with a potential buy-out by Electricité du
528 France (“EDF”), this buy-out however required the approval by Maryland Public Service
529 commission (“MDPSC”). At this point the MDPSC, concerned with the state of BGE,
530 imposed many ring-fencing conditions between Constellation and BGE regarding board
531 control, bankruptcy protection, and legal separation of the entities (many of the
532 conditions similar to what I have proposed in DPU Exhibit 3.3 DIR), essentially creating
533 a strong ring-fence between Constellation and BGE where there had not been one
534 previously. This created a revision and ratings separation between Constellation and BGE
535 by S&P of two (2) notches, with Constellation’s long-term debt being assigned BBB- and
536 BGE’s long-term debt being assigned a BBB+.⁵⁸ The market could now differentiate
537 Constellation’s risky behavior from BGE’s more stable business.

⁵⁶ http://www.baltimoresun.com/bs-mtblog-2008-08-credit_agency_downgrades_bge_p-story.html.

⁵⁷ “Constellation won’t make a specific commitment [to implement robust ring fencing] until we know what the outcome of [the EDF] transaction is.” Transcript of Hearing at 439 (Michael Wallace, Vice Chairman and Chief Operating Officer, Constellation Energy), *In re Balt. Gas & Elec. Co.*, Case No. 9173, Phase II (Md. Pub. Serv. Comm’n., Sept. 15, 2009) (“Case 9173 Transcript”).

⁵⁸ <http://www.fortnightly.com/fortnightly/2010/08/constellation-experience?page=0%2C0>.

538

539 **Q. Do ratings agencies have specific policies or criteria concerning ring fencing**
540 **subsidiaries?**

541 A. Standard and Poor's and Moody's both have ratings criteria and specific guidelines when
542 it comes to ring fencing, S&P looks at a ring fence as:

543 Any action that state regulators take that provides support (whether legal,
544 regulatory, financial or operational) to the utility and/or isolates the utility (most
545 importantly financial obligations) from its parent company will be positive for
546 credit.⁵⁹

547

548 They also have specific guidelines for how they rate parent companies and subsidiaries:

549 Under Standard & Poor's rating criteria: a non-ring-fenced subsidiary cannot be
550 rated above the credit quality of the consolidated entity. A subsidiary that meets
551 Standard & Poor's ring fencing criteria can be rated up to three notches above the
552 credit quality of the consolidated entity, if the underlying economics of the
553 subsidiary support a higher rating.⁶⁰

554 This implies that Standard and Poor's and Moody's both seek out ring fencing provisions
555 when analyzing parent companies, their subsidiaries and potential mergers. The ratings
556 agencies actively look for enforceable ring fencing provisions from regulatory bodies.

557

558 **Q. Dominion and Questar outlined statements of intent in their filing, similar to some**
559 **of the ring fencing conditions outlined in your proposal such as “Dominion and its**
560 **subsidiaries will continue to honor the WEXPRO Stipulation and Agreement” and**
561 **“Dominion is committed to the environment and will maintain the environmental**

⁵⁹ <http://www.ferc.gov/CalendarFiles/20061207112603-Baum,%20Oregon%20PUC.pdf>. Page 5.

⁶⁰ http://www.bondsonline.com/print/Todays_Market/Credit_Rating_News_.php?DA=view&RID=12460.

562 **monitoring and maintenance programs of Dominion Questar Gas at or above current**
563 **levels.” Are all these conditions necessary if there are statements of intent?**

564 A. While statements of intent by Dominion and Questar add a sense of security relative to
565 the impact of the Merger, the Commission, in its protective duties, should act in a more
566 diligent and independent manner. The Commission should make the statements
567 enforceable conditions to the Merger approval. This will help alleviate future debate as to
568 the nature and detail of the statements of intent through clear regulatory conditions and
569 assure that the protections promised are material and have the intended effect. Further,
570 statements of intent are seen by ratings agencies as much less substantial compared with
571 enforceable conditions prescribed by a government commission.

572

573 **Q. The ring fencing conditions mentioned in DPU Exhibit 3.3 DIR could be considered**
574 **onerous on Dominion and Questar post-merger, are all the ring fencing conditions**
575 **critical to protecting customers, what about the costs of implementing and**
576 **maintaining the ring fencing conditions?**

577 A. While it’s impossible to protect from all possible outcomes I view the list presented in
578 DPU Exhibit 3.3 DIR as the best attempt to protect customers from adverse outcomes
579 associated with a lack of ring fencing. The goal of ring fencing is not to make the utilities
580 bankruptcy proof but “bankruptcy remote”.⁶¹ As for the costs associated with
581 implementing and maintaining this ring fencing, the goal is to protect the utility which is
582 deemed effectively the only service provider in the area able to provide an essential

⁶¹ http://papers.ssrn.com/sol3/papers.cfm?abstract_id=406781.

583 service, if there were to be a large-scale disruption or cost increase to this service the
584 aggregate impact to customers would likely greatly exceed the benefit to Dominion and
585 Questar of not implementing these ring fencing conditions.

586 The very fact of a utility company being a monopoly effectively creates a
587 structural mandate for ring-fencing: the utility company should be protected from
588 risk because it is the only entity in its service area able to provide essential
589 services. *The benefits of ring fencing utility companies that are monopolies are*
590 *therefore likely to exceed the costs.*⁶²

591

592 **VII. Review of Proposed Merger Transaction and Transition Costs**

593 **Q. Have the Joint Applicants provided a list and description of proposed transaction**
594 **costs?**

595 A. Yes. The Joint Applicants have provided Merger transaction costs in the Joint
596 Application, Direct Testimony of witnesses Diane Leopold and Fred Wood, and in
597 several responses to discovery questions in both the Utah and Wyoming dockets.

598

599 **Q. Please describe the proposed Merger transaction costs of Questar Corporation.**

600 A. The Merger transaction costs that Questar Corporation, not any affiliates, will be
601 responsible for as a result of the Merger are grouped into the following categories⁶³:
602 financial advisory services, legal expenses, acceleration of financing costs, and
603 miscellaneous costs (include proxy filing, shareholder vote, etc.).

604

⁶² http://www.bondsonline.com/print/Todays_Market/Credit_Rating_News_.php?DA=view&RID=12460.

⁶³ See Questar Gas Company's response to DPU 3.01.

605 Financial advisory services are estimated at \$21.5 million and are costs required to cover
606 investment banking fees that were charged for brokering the Merger. Legal expenses are
607 listed at approximately \$5 million, which is an estimate based on current information, but
608 could change depending on the outcome of shareholder lawsuits. These expenses cover
609 the costs of third party law firms that brokered the Merger and costs of shareholder
610 lawsuits. Not included in these expenses are the third party legal costs for regulatory
611 proceedings in Utah, Wyoming, and Idaho. Acceleration of financing costs are estimated
612 at about \$2.2 million and include Questar Corporation debt financing, which was
613 cancelled due to the Merger, as well as acceleration of executive compensation costs that
614 were not estimated due to uncertainty as to how to reasonably calculate the potential
615 costs. Lastly, miscellaneous costs are estimated at around \$2.0 million and include
616 expenses related to preparing the proxy filing and shareholder vote, which generally
617 include costs like printing, third party consultant costs, etc.⁶⁴

618

619 **Q. Please describe the proposed Merger transaction costs of Dominion.**

620 A. The Merger transaction costs that Dominion, not any Questar affiliates, will be
621 responsible for as a result of the Merger are legal expenses estimated at around \$1.5
622 million and merger-related filing costs estimated at around \$70 to \$90 million.⁶⁵ There is
623 no specific description for each of these costs.

624

⁶⁴ See Questar Gas Company's responses to DPU 3.01 and OCS 2.24.

⁶⁵ See Dominion's response to OCS 2.10.

625 **Q. Are there any other costs that should be considered transaction costs?**

626 A. Yes. Other expenses that should be considered costs of this Merger are the following:
627 potential contribution of up to \$75 million towards full funding of Questar Corporation's
628 ERISA-qualified defined benefit pension plan and Questar Corporation's nonqualified
629 defined-benefit pension and post-retirement medical and life insurance (other post-
630 employment benefit ("OPEB")) plans; an acquisition premium or goodwill cost; and an
631 increase of \$1 million per year for at least five (5) years for charitable contributions
632 within the Dominion Questar Gas service areas.⁶⁶

633
634 Dominion is voluntarily contributing up to \$75 million towards Questar's pension and
635 OPEB plans, based on commercially reasonable efforts, since they are currently
636 underfunded. The reason for aiding in funding the plans is because a portion of the under-
637 funding obligation is attributable to Questar Gas operations. By reducing these pension
638 expenses, Dominion is lessening the costs that would be passed on to Questar Gas
639 ratepayers as a consequence of the under-funding.⁶⁷

640
641 In response to OCS data request 2.06, Dominion defines goodwill as "an asset
642 representing the future economic benefits arising from other assets acquired in a business
643 combination that are not individually identified and separately recognized". It will be

⁶⁶ Joint Application, pp. 26, 28-29.

⁶⁷ Direct Testimony of Fred Wood, pp. 14-15, 18.

644 based on the “fair value”⁶⁸ of Questar’s identifiable assets and liabilities at the closing
645 date of the Merger and the valuation will be determined by a third party.⁶⁹

646
647 As one of Dominion’s commitments of the Merger, it is increasing the corporate level of
648 charitable contributions within Dominion Questar Gas’ service territories by \$1 million
649 per year for at least the next five (5) years. In addition, Dominion explains that it will
650 maintain, if not increase, community involvement, funding for low income customers,
651 and economic development efforts of the current areas of operation of Dominion
652 Questar.⁷⁰

653

654 **Q. Do you agree that the pension contribution will provide timely and quantifiable**
655 **customer benefits?**

656 A. No, for at least three reasons. First, the Joint Applicants seem to have left themselves
657 some flexibility to call the pension contribution a “transition” cost and seek its recovery
658 later from customers. In response to DPU 3.08 when asked to clarify and list “transition
659 costs”, the Joint Applicants provided a non-exclusive list that stated:

660 Other costs could include severance payments to employees, changes to
661 signage, and changes to employee benefit plans, costs to terminate any
662 duplicative leases, contracts and operations, etc.⁷¹

663

⁶⁸ See Dominion’s response to OCS 2.08. Fair value is “the price that would have been received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.”

⁶⁹ See Dominion’s response to OCS 2.06.

⁷⁰ Joint Application, p. 29. Direct Testimony of Diane Leopold, p. 16.

⁷¹ See Questar Gas Company’s response to DPU 3.08 (emphasis added).

664 It's unclear from the response whether "changes" to plan funding levels would qualify as
665 a transition cost, but the Joint Applicants may argue later that it should. If the pension
666 donation can be later recovered in rates, then it is really not a benefit from the Merger.

667
668 Second, the amount of the contribution and its benefit as a rate reduction is uncertain. In
669 response to DPU 3.05, the Joint Applicants noted that the \$75 million was not a firm
670 commitment level, only that the Joint Applicants would use commercially reasonable
671 efforts to make a contribution.⁷² So, actual additional funding could be materially lower,
672 which would reduce any assumed benefit.

673
674 Finally, while the Joint Applicants estimate a \$2.66 million reduction in Questar Gas
675 expense as a result of a full \$75 million contribution in the response to DPU 3.05,⁷³ when
676 and if customers see any actual reductions to rates from a lower estimate expense level
677 entirely depends on rate case timing and the timing of the additional pension funding.
678 For example, the cost of service in the pending Questar Gas rate case would have a
679 pension expense set at pre-Merger levels, so could not reflect any reductions made after
680 the Merger. In fact, if pension expense goes down in the rate year because of increased
681 funding, Questar Gas will stand to benefit in the near term since it will be collecting the
682 pre-Merger (and presumably higher) level of pension expense in rates from customers.
683 This over-collection will persist until the Questar Gas files another rate case sometime in
684 the future. In sum, it is speculative to say that customers will see any benefit from the

⁷² See Questar Gas Company's response to DPU 3.05.

⁷³ *Ibid.*

685 additional funding level for some time, and could experience years of overpaying pension
686 expense based on stale test year expense figures.

687

688 **Q. How do the Joint Applicants plan to treat all of the transaction costs described**
689 **above?**

690 A. The Joint Applicants state that Dominion Questar Gas “will not seek recovery of any
691 acquisition premium (goodwill) cost or transaction costs associated with the Merger from
692 its customers”.⁷⁴ Further, Dominion states that it “will not record any portion of the cost
693 to acquire or any purchase price allocation adjustments (including goodwill) associated
694 with the Merger on Dominion Questar Gas’ books and is planning to make the required
695 accounting entries associated with the Merger on that basis”.⁷⁵ All of the incurred and
696 expensed corporate level⁷⁶ transaction costs that are Merger-related will not be passed
697 down to the Questar affiliates. In addition, if the Merger were terminated, costs will be
698 assigned to Dominion and Questar based on “Section 7.3 of the Agreement and Plan of
699 Merger”.⁷⁷ Again, Questar Corporation would be responsible for the termination fee, and
700 no costs would be borne by its subsidiaries.⁷⁸

701

702 **Q. Do you agree that all transaction costs should be paid for by the Joint Applicants**
703 **regardless if the Merger occurs or is terminated?**

⁷⁴ Joint Application, p. 28. Direct Testimony of Fred Wood, p. 17. See Dominion’s response to OCS 2.06, OCS 2.11, and WPSC 2.08.

⁷⁵ *Ibid.*

⁷⁶ Refers to Questar Corporation and Dominion.

⁷⁷ See Dominion’s response to WPSC 1.05.

⁷⁸ *Ibid.*

704 A. Yes. Both corporate levels of each Company should be responsible for the transaction
705 costs and not the affiliates, especially Questar Corporation’s affiliates. Further, all costs
706 indicated in this testimony as transaction costs should be classified as transaction costs
707 and therefore not eligible for recovery. Transaction costs, whether incurred before or after
708 the Merger should be treated the same, ineligible for recovery.

709
710 **Q. Have Dominion and Questar provided a list and description of proposed transition**
711 **costs?**

712 A. Partially. In response to DPU data request 3.08, Questar Gas Company defines transition
713 costs and provides examples of what transition costs include. However, the Joint
714 Applicants cannot “identify with specificity”⁷⁹ all transition costs beyond the examples
715 and stated that “[n]o transition costs have currently been quantified”.⁸⁰ Further, Questar
716 Gas explains that “[a]s the specifics of the integration process become more clearly
717 defined, the parties will have a better understanding of the impacts they will have on
718 costs”.⁸¹

719
720 **Q. Please describe the proposed Merger transition costs of Questar Corporation.**

721 A. Questar Gas Company defines transition costs as “expenditures resulting from the
722 preparation and implementation of activities necessary to integrate the purchased entity
723 into the acquiring entity”.⁸² Further in the response, Questar Gas Company provides

⁷⁹ See Dominion’s response to OCS 2.12.

⁸⁰ See Questar Gas Company’s response to DPU 6.04.

⁸¹ *Ibid.*

⁸² See Dominion’s response to DPU 3.08.

724 examples of transition costs, which include the following: “integration of financial, IT,
725 human resource, billing, accounting, and telecommunication systems”; “severance
726 payments to employees, changes to signage, and changes to employee benefit plans, costs
727 to terminate any duplicative leases, contracts and operations, etc.”⁸³

728
729 The one transition cost that has some quantitative evaluation behind it is severance costs,
730 especially for executives of Questar Corporation. In Questar Corporation’s response to
731 DPU data request 4.02, Questar Corporation explains the payments and benefits that
732 officers of Questar Corporation and Questar Gas will receive “upon a qualifying
733 termination within 3 years following a change in control event”.⁸⁴ This benefits package
734 applies only if termination of employment occurs without “cause” or the employee leaves
735 for “good reason”. All other employees, outside of the executives, will become subject to
736 the severance policy of Dominion based on their full time or part time employment
737 status.⁸⁵ The most current estimate of the executive severance compensation, dated May
738 19, 2016, which would be in effect for all Questar Corporation and Questar Gas
739 executives upon change in control, is approximately \$15 million in total.⁸⁶

740
741 One other transition cost not directly included in the above list is employment transition
742 costs, which include employee transfer costs and employee benefit plans (including Paid
743 Time-Off Plans, 401(k), and pension plans). As with the other transition costs, Dominion

⁸³ *Ibid.*

⁸⁴ See Questar Corporation’s response to DPU 4.02.

⁸⁵ *Ibid.*

⁸⁶ See Questar Corporation’s response to DPU 6.69.

744 has not estimated any costs related to these expenses. The main reason is because
745 “Dominion and Questar have not yet determined the synergies that will result when the
746 shared or common services functions at Questar Corporation and Dominion Resources,
747 Inc. are combined”.⁸⁷ For each of the employee benefit plans, Dominion explains that it
748 does not have any current decisions that have been finalized and it is still evaluating
749 options.⁸⁸

750

751 **Q. Were the Joint Applicants able to quantify transition costs?**

752 A. No. As explained in the discussion above, the Joint Applicants were not able to identify
753 specific transition costs, outside of severance costs, and therefore were not able to
754 quantify these costs. Instead, Dominion states that “as we move through the transition
755 process, the details of costs, how the costs fall into the ‘transition cost’ category,
756 accounting details (FERC account and sub accounts to which they may be charged) will
757 be developed as part of the transition process”.⁸⁹

758

759 **Q. Did the Joint Applicants perform any studies to identify transition costs and/or**
760 **calculate their benefits to customers?**

761 A. No. The Joint Applicants did not perform any studies to identify transition costs and did
762 not calculate any net benefits of transition costs to customers. There were multiple data
763 requests propounded to the Joint Applicants inquiring about the identification and

⁸⁷ See Dominion’s response to DPU 4.09. Stated similarly in the Joint Application, p. 12.

⁸⁸ See Dominion’s response to OCS 2.55, OCS 2.58, and OCS 2.62.

⁸⁹ See Dominion’s response to OCS 2.12.

764 quantification of transition costs related to the Merger.⁹⁰ The responses to the data
765 requests mostly directed investigators back to DPU data request 3.08, which defined and
766 listed examples of transition costs. Even when asked if Dominion “studied the mergers of
767 other holding companies and/or utilities to identify and/or quantify transaction costs,
768 transition costs and/or synergy savings”, Dominion explained that it did not study any
769 other mergers.⁹¹ In another data request, Dominion was asked to provide any formal
770 studies, analysis, or reports regarding the integration of Questar into its organizational
771 structure. Again, Dominion responded that no reporting or studies on the integration has
772 been done to date.⁹² Questar Corporation and Dominion were asked to provide due
773 diligence reports, synergy studies, net savings studies, and integration plans. Questar and
774 Dominion, except for a due diligence report, did not prepare any of these studies, plans,
775 or reports.⁹³

776
777 After review of the Joint Application, Direct Testimonies, and data requests responses
778 from Dominion and Questar, it is apparent that there was a lack of reports and studies
779 done in order to quantify customer benefits and transition costs. The approach taken by
780 the Joint Applicants appears to be a “trust us” approach based on this apparent lack of
781 analysis and Dominion’s response to DPU data request 6.03, which sums up how
782 Dominion feels about the benefits and savings of the Merger:

⁹⁰ See Dominion’s responses to OCS 2.12, OCS 2.13, OCS 2.15, OCS 2.17, OCS 2.18, and DPU 6.02. See Questar Gas Company’s responses to DPU 3.08, DPU 6.04, DPU 6.05, and DPU 6.22. See Questar Corporation’s responses to DPU 6.01 and DPU 6.70.

⁹¹ See Dominion’s response to OCS 2.20.

⁹² See Dominion’s response to OCS 2.15.

⁹³ See Questar Corporation’s response to DPU 6.01 (f-i). See Dominion’s response to DPU 6.02 (f-i).

783 As discussed in the Joint Application and testimony, the Joint Applicants’
784 rationale for the proposed Merger is premised on the ability to grow Dominion’s
785 and Questar’s regulated infrastructure profile and is not focused on achieving cost
786 reductions (please refer to the response to DPU 3.03 for additional discussion on
787 this topic). Though a formal synergy study is not planned and expected synergy
788 savings have not been specifically estimated, the Joint Application (including
789 testimony and exhibits), the Joint Applicants’ presentations at the April 28th and
790 29th technical conferences in Utah and Wyoming respectively, and Joint
791 Applicants’ responses to discovery, taken together:

- 792 • Explain the benefits and savings expected to result over time;
793 • Present numerous commitments and understandings that will be of
794 substantial value to and protective of Dominion Questar Gas’ customers,
795 employees and communities in future years; and
796 • Demonstrate that the Merger is clearly in the public interest.⁹⁴

797

798 Although the Joint Applicants explain there are several potential benefits⁹⁵ and savings to
799 Questar Gas and its ratepayers from the Merger, there is no formal quantitative analysis
800 provided to back up the statements. Dominion explains that benefits from the Merger are
801 expected as have been presented in the sources above, even though no net benefits have
802 been estimated.⁹⁶

803 **Q. How do the Joint Applicants plan to treat all of the transition costs described above?**

804 A. In the Joint Application, Questar requested “the Commission to issue an accounting order
805 authorizing it to defer transition costs incurred in connection with the Merger, if it
806 chooses to do so, for later recovery if deemed appropriate by the Commission”.⁹⁷ The

⁹⁴ See Dominion’s response to DPU 6.03 (a-c).

⁹⁵ Joint Application, pp. 29-31, paragraph 59 (a-j).

⁹⁶ See Dominion’s response to DPU 6.03 (f).

⁹⁷ Joint Application, p. 2. Restated at the end of the Joint Application on p. 35.

807 transition costs that would be deemed eligible for recovery are the costs where Dominion
808 Questar Gas can demonstrate the net benefit to customers due to the costs.⁹⁸

809
810 Dominion Questar Gas plans to track the transition costs by creating a deferred asset
811 account, if approved by the Commission.⁹⁹ In response to WPSC data request 2.13,
812 Dominion explains that the transition costs and transition savings are going to be tracked
813 for about one year following the close of the Merger, with the transition savings being
814 tracked “concurrent with related costs”.¹⁰⁰ Besides tracking the costs and savings,
815 Dominion Questar Gas needs to calculate the net benefits of the transition costs in order
816 for the Commission to approve them. When asked for the proposed methodology for
817 calculating net benefits, Dominion responded that “[t]he methodology for calculating the
818 net benefit will be developed as part of the transition process”.¹⁰¹

819

820 **Q. Do you agree with how transition costs are planned to be treated by the Joint**
821 **Applicants?**

822 A. No. First, the Joint Applicants need to provide or do more analysis that demonstrates net
823 benefits of the Merger to Questar Gas and its customers, as explained by the Joint
824 Applicants in response to several data requests. As a result, there is no way to properly
825 analyze the impacts of these transition costs on ratepayers until long after the Merger is

⁹⁸ Joint Application, p. 28. Direct Testimony of Fred Wood, p. 17. See Questar Corporation’s responses to DPU 4.09 and DPU 6.70. See Dominion’s response to OCS 2.13 (c).

⁹⁹ See Questar Gas Company’s response to DPU 3.08.

¹⁰⁰ See Dominion’s response to WPSC 2.13.

¹⁰¹ See Dominion’s response to OCS 2.13 (d).

826 complete. Second, the methodology for calculating net benefits, required to document
827 savings in addition to costs, has not even been considered. Again, there is no way to
828 properly analyze the methodology used to calculate net benefits until after the Merger has
829 been completed.

830
831 Third, transition costs related to synergies resulting from the combination of services
832 offered by Questar Corporation and Dominion Resources Services, Inc. have not yet been
833 determined.¹⁰² These service changes include “investor relations, governance, finance,
834 treasury, tax, accounting, legal, IT, telecommunications, insurance, purchasing,
835 contracting, environmental management, safety, audit, and human resources.¹⁰³ Along
836 with these services, several current Questar Corporation employee jobs will most likely
837 be terminated during its integration into Dominion which may lower the costs of
838 Dominion Questar Gas services over time. However, there is no proper way to analyze
839 these costs before the Merger is approved without information from the Companies and
840 this is compounded by the lack of a methodology to calculate the net benefits.

- 841
- 842 **Q. Do you have a recommendation for how the Commission should treat transition**
843 **costs?**
- 844 A. Yes. The Commission should deny recovery of all transition costs. The Companies claim
845 several benefits of the Merger, but have not sufficiently shown any reports or studies for
846 evaluating and quantifying transition costs and have not proposed any methodology for

¹⁰² Joint Application, p. 12.

¹⁰³ *Id.*, pp. 11-12.

847 calculating net benefits to ratepayers. Furthermore, transition costs, like transaction costs,
848 are necessary expenses the acquiring Company is incurring in order to merge with the
849 acquired Company. Ratepayers should not be held responsible for these acquisition and
850 integration costs, when the latter have yet to be fully analyzed by the Joint Applicants.

851

852 **Q. If the proposed transaction is to be approved, what provisions would you**
853 **recommend be established by the Commission in relation to transaction and**
854 **transition costs?**

855 A. If the Commission approves the Merger, there is a list of conditions regarding transaction
856 and transition costs that it should establish that are listed below: (Additional Merger
857 Conditions are included in DPU Exhibit 3.4 DIR).

- 858 • Deny direct or indirect recovery of an acquisition premium in any form,
859 including but not limited to the write-up of assets or goodwill.
- 860 • Identify all transaction and transition costs in its accounting system.
- 861 • Deny recovery of all transaction costs regardless of whether incurred before or
862 after transaction closes.
- 863 • Deny deferral of transition costs.
- 864 • Deny recovery of any transition costs.
- 865 • For the next five years, limit recovery of costs and investments to projections
866 existing prior to the merger without Commission pre-approval.
- 867 • Deny recovery of all severance costs.

- 868 • Deny recovery of all investment costs incurred to installation of new systems
869 or integration of existing systems due to merger.
- 870 • Require the filing for review and approval of the merger integration study
871 materials and final integration plan within 12 months following the
872 consummation of the merger.
- 873 • Require the acceleration of financing costs and executive compensation costs
874 that were not estimated due to uncertainty as to how to reasonably calculate
875 the potential costs to be clearly stated and capped.
- 876

877 **VIII. Merger Savings Credit**

878 **Q. Did the Joint Participants filing describe the quantifiable net benefits to customers?**

879 A. As discussed above, neither the Joint Application nor the responses to discovery
880 scrutinizing this issue revealed that the Joint Applicants performed the necessary studies
881 to provide a reasonably reliable quantification of net benefits to customers.

882

883 **Q. Did the Joint Participants filing describe the benefits to shareholders of the proposed**
884 **Merger?**

885 A. They did not describe the quantifiable benefits to shareholders in great detail in the Joint
886 Application. There is mention of the Merger transaction details in the filings and general
887 acknowledgement that shareholders will benefit, but there is no estimate or detailed
888 discussion of earnings or share value accretion due to the Merger. The lack of
889 comprehensive analysis of shareholder benefit in the Joint Application beyond aspirational

890 generalities is somewhat troubling since it is highly unlikely management would propose
891 such a radical change in ownership as a merger of the Joint Applicants without confidence
892 that shareholders would profit.

893 **Q. Why do you believe the Joint Applicants should have studied the shareholder benefits**
894 **of the Merger with more quantified detail than described in the Joint Application?**

895 A. The Merger represents a significant investment in the acquisition of another company and
896 its subsidiaries, and a business case should have been developed demonstrating why the
897 transaction makes sense. According to the Joint Application, Dominion has arranged
898 financing to “immediate access to cumulative funds of up to \$4.4 billion, sufficient to
899 satisfy 100 percent of the amount required to fund the exchange of the shares of Questar
900 Corporation for cash.”¹⁰⁴ If the circumstances of the investment were changed and the
901 Dominion planned to investment \$4.4 billion in new generation stations, for example, the
902 need for, and estimated cost of, the plants would have been well developed and explained
903 to the Commission before the Company sought regulatory approval for cost recovery. To
904 do otherwise would expose the utility to the risk that the Commission may deny some
905 recovery as not well supported during a prudence review.

906

907 **Q. Have the Joint Applicants studied the issue?**

908 A. [REDACTED]

909 [REDACTED]

910 [REDACTED]

911 [REDACTED]

¹⁰⁴ Joint Application p. 10.

912
913
914
915
916
917
918
919
920
921
922
923
924
925
926
927
928
929
930
931
932

933

934
935
936
937

938

939
940
941
942

943

[REDACTED]

944 **Q. What are some of the ways shareholders can benefit from the merger that the Joint**
945 **Applicants have not quantified in the Joint Application?**

946 A. Shareholders can benefit in at least three ways. First, through rate case timing, the Joint
947 Applicants could file for distribution rate increases early in the Merger integration process
948 when Merger costs are abundant and then potentially enjoy higher earnings in the later
949 years as any Merger-enabled savings ramp up, assuming savings materialize.

950
951 Second, if the Joint Applicants have not finished realizing savings and passed them along
952 to customers in rates, a third party entity would have incentive to propose a follow-on
953 merger transaction and offer shareholders an acquisition premium that represents, at least
954 in part, the unrealized savings from the current merger.

955 Third, the Joint Applicants have requested the deferral for later recovery of Merger
956 transition costs¹⁰⁵, so the financial risk of integrating the combined companies is reduced,
957 since without the deferral, otherwise recoverable transition expenses could not be
958 recovered from customers in rates unless the costs accrue in a test year. So, shareholders
959 have ample opportunities to benefit from the new corporate entity.

960
961 **Q. Can utility mergers similar to the one proposed by the Joint Applicants generally**
962 **produce benefits for customers or ratepayers?**

963 A. Yes. Utility mergers can provide stipulated benefits (or benefits that are anticipated to be
964 passed along to ratepayers at a future time as management decisions, operational changes,

¹⁰⁵ Joint Application p. 2.

965 and additional investments take place) and/or actual benefits that are passed along at the
966 time of the approval of the merger. The key here, of course, is the implementation of an
967 appropriate regulatory structure that ensures savings are passed along to customers. In the
968 present case, although the Joint Applicants have not provided any quantified net savings
969 figure, that savings opportunities for ratepayers are not necessarily absent.

970

971 **Q. By what mechanism will economic benefits be passed on to ratepayers?**

972 A. Although the Joint Application discusses generally that bills may be lower than they
973 would be without the proposed merger,¹⁰⁶ the Joint Applicants have not proposed any
974 rate changes at the current time. It is possible that rates may be lowered through a future
975 rate proceedings, though the timing of those proceedings and other possible future rate
976 mechanisms to capture merger-related savings remains unknown and therefore cannot be
977 relied upon as a supporting factor in reviewing this merger. Also, if certain costs are
978 reduced, it is important to ensure that leeway is not given for costs to increase in another
979 category to be placed into rates again.¹⁰⁷ For cost savings to be truly beneficial to
980 ratepayers, they need to be permanent in some capacity over time.

981

¹⁰⁶ Join Application p. 12.

¹⁰⁷ For example, if as part of the merger integration, a company reduces employees at the service company level, but then rehires some of those former employees as outside consultants or hires third parties to perform the same services as the dismissed employees, the Company cannot count as “savings” the initial reduction in salary expense without also factoring in the payments made for the replacement services.

982 **Q. Do you see any reasons that the Joint Applicants would not be able to provide a**
983 **commitment to transfer the projected net economic benefits to ratepayers at the**
984 **current time?**

985 A. No. I believe that the lack of a concrete evaluation of net savings estimates provided by
986 the Joint Applicants combined with the request for transition cost deferral creates a
987 substantial uncertainty for rate payers associated with the transaction. The Joint Applicants
988 should commit to a rate mechanism now that allows customers to realize definite savings
989 up front, especially in light of the Joint Applicants request to apply for the collection of
990 Merger-related transition costs in a future rate case.¹⁰⁸ The Joint Applicants have stated in
991 their filings that the extent and timing of cost-recovery, and presumably rate changes that
992 incorporate any Merger-related net savings, are not part of the current proceeding.¹⁰⁹ I
993 agree that the Joint Applicants have not sought to pass on savings in the current proceeding,
994 but if the Commission is inclined to approve the Merger, I see no reason why the
995 Commission should not condition its approval of the Merger to include a requirement that
996 the Joint Applicants offer an adjustment to revenue requirements that accounts for both
997 Merger-related costs and savings, assuming the savings outweigh the costs when calculated
998 into rates. Though ideally this adjustment should occur immediately upon Merger closing,
999 one might also consider such timing to occur when the Dominion Questar Gas files its next
1000 rate proceeding.

1001 Such an adjustment, which I label the Merger Savings Credit (“MSC”), would incorporate
1002 a Merger-related net savings in a way that represents a meaningful commitment from the

¹⁰⁸ Joint Application p. 2

¹⁰⁹ *Id.*, p. 12.

1003 Joint Applicants to pass assured savings along to customers and incent the necessary
1004 management actions to implement these savings expeditiously.

1005

1006 **Q. Please describe how the MSC would work.**

1007 A. As part of their next base rate proceeding, Dominion Questar Gas would provide customers
1008 with a distribution rate reduction to better align costs with savings. With a well-supported
1009 Merger filing, I would recommend calculating the MSC by starting with a review of robust
1010 estimates of projected savings and the associated costs to achieve them over time. To
1011 calculate the appropriate credit, first I would generated an estimate of net savings. By, then
1012 I would amortizing amortize the savings in a similar manner to costs, and finally I would
1013 and netting net them the amortized savings against amortized transition costs, to produce
1014 the resulting figure would be the MSC. Given the uncertainty around the Joint Applicants'
1015 quantifiable savings, the Joint Applicants are obliged to protect customers and should be
1016 able to at least provide this minimum level of net savings to ratepayers. At the same time,
1017 the Joint Applicants could enjoy benefits if they provide higher net savings levels (either
1018 by reducing Merger-related costs or increasing Merger-related benefits), and the MSC
1019 adjustment would provide incentives for them to do so.

1020

1021 In this case, however, the Joint Applicants have not provided projected costs and savings
1022 studies in the Joint Application. Under these circumstances, it would be appropriate to
1023 use industry average merger-related savings to calculate an initial MSC that could be
1024 applied now to distribution rates pending a review of actual costs and savings in the next

1025 rate proceeding. As discussed in more detail below, utility mergers can produce savings
1026 of up to 5% on non-fuel O&M expenditures.¹¹⁰

1027

1028 **Q. Have the Joint Applicants announced definitive dates for filing rate base proceedings**
1029 **for the Joint Applicants.**

1030 A. Questar Gas filed a rate case July 1, 2016. Consequently, I recommend that the an imputed
1031 merger credit of 5% of the non-Fuel O&M amount included in the test year provide the
1032 initial MSC and be effective as of January 1, 2017. The initial MSC will persist in rates
1033 until reexamined with the next base rate case following the integration process, but should
1034 serve as floor on the MSC going forward in order to provide incentives for efficient
1035 operations and ensure customer benefits.

1036 **Q. Why did you select January 1, 2017 as the date to apply the credit?**

1037 A. This date will provide some opportunity for the Joint Applicants to begin the integration
1038 process that should result in cost reductions, and also will provide customers with some
1039 minimum level of immediate benefits. Since the Company just filed a rate case with a pre-
1040 merger test year, once the integration process is underway, the test year will almost
1041 certainly become “stale.” In other words, the selected test year will unlikely not be
1042 representative of costs on a gong forward basis as integration is underway.

1043

1044 **Q. What are the benefits of the MSC?**

¹¹⁰ See Section IX, supra.

1045 A. First, the MSC addresses the problem of regulatory matching of the costs and savings from
1046 the Merger. An upfront benefit is that customers benefit upfront will have from receiving
1047 a commitment from the Joint Applicants that the anticipated Merger-related benefits will
1048 flow back to them. Since the interests of the Joint Applicants, customers, and shareholders
1049 are balanced because the latter will see substantial benefits from the transaction,¹¹¹
1050 providing the up-front credit helps balances the interests of shareholders and customers
1051 over time. As discussed above, the current standard of review requires a showing of net
1052 benefits, a distribution rate reduction will satisfy this requirement. The expectation should
1053 be that the initial imputed credit will provide a floor for the amount of net economic
1054 benefits to be included in rates until reexamined in the context of next rate case. The
1055 presumption must be, however, that the costs would not increase or else the Joint
1056 Applicants will have incentives to increase Merger related costs to overtake savings over
1057 time. There should be incentives for cost reductions to endure.

1058
1059 Second, the MSC would apply for a number of years following the Merger thus mitigating
1060 the problem associated with follow-on mergers diverting unrealized savings from this
1061 Merger into an acquisition premium for the next. For example, should the next merger
1062 involve a holding company over which the Commission has no jurisdiction and another
1063 state does have jurisdiction over the merger approval, it may be difficult to ensure that
1064 Dominion Questar Gas ratepayers continue to receive an appropriate share of merger-
1065 related savings.

¹¹¹ See Dominion's response to DPU 6.02 a-b, pp. 23, 81.

1066

1067 **Q. Are you proposing the actual MSC tariff with your testimony?**

1068 A. Not at this time, although I am proposing an initial imputed merger rate credit. As a
1069 condition of the merger approval, however, the Joint Applicants should file the appropriate
1070 proceeding within 12 months following the end of the currently anticipated rate case to
1071 create the tariff for the MSC in accordance with the guidelines outlined in this testimony.
1072 The MSC application should be adequately supported with prefiled testimony describing
1073 the actual costs and savings, the merger integration plans, areas studied for savings and
1074 progress among the integration timelines for each business function, as well a proposed
1075 tariff, all for review and approval by the Commission.

1076

1077 **IX. What Concerns Should the Commission Have Regarding the Proposed**
1078 **Transaction?**

1079 **Q. The proposed transaction is an acquisition by a parent utility holding company of**
1080 **another parent utility holding company. How will this transaction, if approved,**
1081 **affect Dominion Questar Gas, which would be regulated by the Commission?**

1082 A. The Joint Applicants have stated that they will not combine any company, in this case
1083 Dominion Questar Gas, regulated by the Commission without Commission approval.
1084 The Joint Applicants have also stated that they have not estimated any savings or
1085 synergies due to the proposed transaction. Thus, it is possible that Dominion Questar Gas
1086 may not be immediately affected by the transaction.

1087

1088 **Q. If the transaction is approved and Dominion Questar Gas, which would be**
1089 **regulated by the Commission, may not be immediately affected by the Merger, why**
1090 **should the Commission be concerned about the proposed Merger?**

1091 A. The Utah utility holding company acquisition standard requires that the Merger be in the
1092 public interest. Without any identified savings to ratepayers, it is difficult to see how this
1093 acquisition could benefit ratepayers and be in the public interest. Moreover, Dominion is
1094 paying an above-market premium to acquire Questar. Investors providing funds to
1095 Dominion to pay this above-market premium are expecting an adequate return. If the
1096 acquisition is approved, Dominion Questar will need to generate increased earnings,
1097 profits, and cash at the parent company level to fund the above-market premium. To do
1098 this, Dominion Questar would likely need to extract higher earnings, profits, and cash
1099 flow from its regulated subsidiaries. Without sufficient synergies or savings that can be
1100 shared equitably between shareholders and ratepayers, these higher earnings and profits
1101 will need to come from higher rates at regulated subsidiaries. The Joint Applicants have
1102 identified none. Thus, it is possible that ratepayers could be harmed by the proposed
1103 transaction if it is approved as proposed. The Commission should be very concerned
1104 about this possibility, especially given the lack of synergies identified by the Joint
1105 Applicants.

1106
1107 **Q. Could synergies offset these higher costs of supporting the Merger premium?**

1108 A. In theory, a transaction could yield enough synergies to offset or exceed the higher merger
1109 costs and still provide benefits to both shareholders and ratepayers. The high end of Mr.

1110 Reed's savings estimate is 5% of non-fuel O&M costs. Not all O&M costs are avoidable.
1111 Using figures from the 2015 Annual Report to the Commission, the imputed merger
1112 savings credit should be \$7.8 million dollars based on non-fuel O&M expenditures of \$156
1113 million.¹¹²

1114

1115 **Q. If the Merger were to be approved as proposed, how could post-acquisition**
1116 **Dominion Questar extract higher earnings, net income, and cash flow from the**
1117 **regulated operating subsidiary level to the parent company level?**

1118 A. One way to achieve this outcome would be to increase dividend payments to the parent.
1119 This means the regulated subsidiaries would retain less cash than would be otherwise
1120 used to invest in utility infrastructure. Another possible mechanism would be to hold
1121 regulated rates at current levels and reduce costs. This will result in higher net income
1122 and facilitate higher cash dividends to the parent. These are just a few examples, and
1123 there are undoubtedly other means that the Applicant could use to achieve this outcome.
1124 Any of these mechanisms for extracting higher earnings, net income, and cash flow from
1125 the regulated subsidiaries could adversely affect Utah ratepayers.

1126

1127 **Q. Have the Applicants provided an assessment of the financial impact of the proposed**
1128 **transaction?**

¹¹² <http://www.psc.utah.gov/utilities/gas/gasindx/2016/1605707indx.html>.

1129 A. As indicated above, the Applicants have provided little evidence of quantitative analysis,
1130 of the information provided even under confidentiality requirements, much has been
1131 redacted.

1132

1133 **Q. If the proposed transaction is to be approved, how can the Commission protect**
1134 **ratepayers from adverse outcomes?**

1135 A. It is probably not feasible to completely protect against 100% of potential adverse
1136 outcomes. One way to mitigate the impact of potential adverse outcomes to ratepayers is
1137 to establish ring fencing provisions that become binding conditions of any approved
1138 acquisition. A ring fencing provision is a condition that creates a ring or a fence around
1139 regulated subsidiaries that protects that entity from the activities and actions of its parent
1140 company and other affiliates. For example, as a condition of approving the proposed
1141 transaction, the Commission could prohibit a regulated subsidiary from loaning money to
1142 or borrowing from its parent. Ring fencing provisions were discussed in an earlier
1143 section of this testimony. Ring fencing provisions are very common in mergers and
1144 acquisitions involving regulated subsidiaries and affiliates. Such provisions have been
1145 described in Section VI of this testimony and DPU Exhibit 3.3 DIR provides detailed ring
1146 fencing conditions for consideration.

1147

1148 **X. Utah Ratepayer Protections**

1149 **Q. Do Dominion or Questar have any ring fencing provisions they deem necessary?**

1150 A. As indicated earlier in this testimony, the Joint Applicants have proposed commitments
1151 for future management and operations.

1152

1153 **Q. Given the potential risks to Utah ratepayers, do you think that the existing ring**
1154 **fencing provisions and the approval conditions identified in the Application are**
1155 **adequate?**

1156 A. No. The existing ring fencing provisions and the commitments by the Joint Applicants
1157 are not adequate. They do not address the potential adverse outcomes that I identified
1158 earlier in this testimony.

1159

1160 **Q. If the Merger is to be approved, what ring fencing provisions would you recommend**
1161 **be established by the Commission?**

1162 A. See Section VI and DPU Exhibit 3.3 DIR for proposed ring fencing provisions.

1163

1164 **Q. If the Merger is to be approved, are there any other conditions you would**
1165 **recommend?**

1166 A. Yes. The ring fencing provisions proposed above are the minimum necessary to reduce
1167 the potential for harm to Utah ratepayers from the proposed transaction. Additional
1168 conditions providing quantifiable benefits to customers are also necessary in order for the
1169 transaction to be deemed to be in the “best interests” of Utah ratepayers (see DPU Exhibit
1170 3.4 DIR for additional conditions of the Merger).

1171

1172 **Q. It is possible that proceedings in Wyoming and Idaho could establish acquisition**
1173 **conditions after the record has closed in this proceeding that could have an impact**
1174 **on Utah?**

1175 **A.** Yes.

1176

1177 **Q. Is there a way for the Commission to protect against any adverse impacts to Utah**
1178 **ratepayers from those proceedings?**

1179 **A.** Assuming the Commission approves the Merger, this Commission could require that that
1180 Applicant offer to Utah any conditions that are ordered or part of a settlement in any
1181 other jurisdiction that reviews the Merger. This condition would be equivalent to a “most
1182 favored nation’s clause” and would ensure that Utah ratepayers are afforded at least the
1183 same level of benefits and protections that are provided to ratepayers in other states;
1184 however this condition on its own should not take the place of the other conditions
1185 discussed in this testimony.

1186

1187 **XI. Conclusion**

1188 **Q. Does this conclude your testimony?**

1189 **A.** At this time, yes, it does. If additional, relevant information becomes available, I will
1190 supplement this testimony as appropriate.