State of Utah
Department of Commerce
Division of Public Utilities

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Memorandum

TO: Public Service Commission

FROM: Division of Public Utilities
Chris Parker, Director,
Artie Powell, Energy Manager
Charles Peterson, Technical Consultant
Doug Wheelwright, Technical Consultant

DATE: August 22, 2013

RE: Questar Gas Dividend Declaration July 30, 2013
Docket 13-999-02

I. RECOMMENDATION – No Action

Based upon the following analysis, the Division finds no indication that the capital and operations of Questar Gas Company will be impaired pursuant to UCA 54-4-27. Therefore, the Division recommends that the Commission take no action.

II. ISSUE

On July 30, 2013 the Board of Directors of Questar Gas Company (QGC) declared a quarterly cash dividend of $8,875,000. The dividend is payable to the Company's sole shareholder, Questar Corporation, on September 9, 2013. On August 1, 2013, the Commission issued an action request to the Division concerning the Questar Gas dividend declaration. This memo is being filed in response to that request

Pursuant to Utah Code Annotated 54-4-27, the Company must notify the Commission of the dividend within five days of its declaration. The Commission has 30 days from the dividend declaration date to investigate whether the payment of such dividend would result in impairment of the capital or to the utility's service to the public, and if it finds that such impairment will or may occur, the Commission may order that the dividend not be paid.

III. ANALYSIS

The Division understands the terms "impaired" and "impairment" in the statute to mean that (1) the payment of the dividend will result in actions being taken against the Company by creditors, rating agencies, or others due to a reduction in the value of the capital, the violation of loan covenants, or other agreements; (2) the payment of the dividend would result in a reduced ability of the Company to provide service through a lack of working capital or other financial capacity to continue its operations in the same manner as it would if the dividend were not paid.

The Division of Public Utilities investigated the effects of the dividend on the capital and cash flows of the Company using the latest financial information available. This included the annual financial statements through December 31, 2012, quarterly financial statements as of June 30, 2013, Questar Corporation News Release dated July 30, 2013, and a review of the Company's bond rating from the various bond rating agencies. The Division has also reviewed and compared the operational statistics for the first six months of 2013 with the same period in 2012.

Exhibit 1 is a summary of the financial results for the periods ending December 31, 2008 through June 30, 2013. Because of the seasonal nature of it business, Questar Gas typically reports income in the first and fourth quarters of the year and losses in the second and third quarters of the year. For the 12 months ending December 31, 2012, total revenue decreased 11.0% from $968.8 million to $862.2 million. The decrease in total revenue corresponds with a 17.4% decrease in the natural gas commodity cost. Wexpro provided 68% of the natural gas supply in 2012 compared to 52% in 2011 and 51% in 2010. The higher Wexpro percentage in 2012 was due to increased production and lower Questar Gas sales volume due to warmer than normal weather conditions.

For the first half of 2013, total revenue was 12.2% higher than the same period in 2012. The increase is primarily due to colder than normal temperatures that occurred in January and February. Net income for the first half of the year was up 9.8% from $32.6 million in 2012 to

$35.8 million through June 2013. Weather, as measured in degree days, was 16% warmer than normal for calendar year 2012 but has been 13% colder than normal for the first half of 2013. While the weather was colder, the temperature adjusted usage per customer decreased 3.8% from 66.4 Dth through June 2012 compared to 63.9 Dth through June 2013.

The balance sheet information on pages 2 and 7 of Exhibit 1 identifies a steady increase in the Net Plant & Equipment from 2008 through 2012 averaging a 5.8% annual increase. Capital expenditures increased from $82.6 million in 2009 to $162.1 million in 2012 partially due to the ongoing feeder line replacement program. Capital expenditures for the first half of 2013 were $74.1 million compared to $85.9 million for the first six months of 2012. The balance sheet information indicates a slight increase in the accounts receivable balance from $63.4 million as of June 2012 to $93.8 million as of June 2013.

Page 4 of Exhibit 1 calculates the financial ratios for the periods under review. Short-term liquidity ratios for year-end 2012 are slightly lower than historical averages with the current ratio at 0.69 and the quick ratio at 0.45 compared to the average of 0.76 and 0.48. The long-term solvency ratios are near the historical averages with Net Worth/Total Debt at 0.42 and Net Worth/Fixed Assets at 0.37.

The profitability ratios are changing with the increase in capital expenditures. Return on Total Assets shows a slight decrease to 4.12% in 2012 compared to the average of 4.38%. Return on Total Capital was 7.89% in 2012, slightly below the average of 7.99%. On an SEC financial reporting basis, the Company had a Return on Equity (ROE) of 10.24% for 2012. The company's authorized return on equity is 10.35% and is calculated based on different regulatory guidelines. On a fully-adjusted Utah jurisdictional basis, Questar Gas's return on equity was 9.02% for year-end 2012[1] compared to 9.84% for year-end 2011.[2] Based on the calculations, the Company does not appear to be earning more than the authorized rate of return.

[1] Questar Gas, Utah Results of Operations, 12 Months Ending December 31, 2012
[2] Questar Gas, Utah Results of Operations, 12 Months Ending December 31, 2011

Included in the Other Financial Indicators section are four calculations used by Moody's as part of their bond rating guidelines. These include the EBIT/Interest, Debt/Book Capitalization, Retained Cash Flow/Debt and a Simple ROE calculation. All of these ratios are within the guidelines specified as of year-end 2012 and for the first six months of 2013. The financial characteristics of Questar Gas generally indicate a profitable and stable utility company.

The Company's regulatory capital structure was 47.70% debt and 52.30% equity as of year-end 2012 which are close to the historical average of 47.36% debt and 52.64% equity. Common equity grew at an average rate of 6.54% for the periods under review and included a $30 million equity contribution from the parent company in 2008 and a $20 million equity contribution in 2011. Common equity for the first six months of 2013 has increased to 55.72%. It is anticipated that with the combination of debt offerings, dividend payments and equity contributions, the Company will maintain an equity position near the historical average of 52%.

Long-term debt is currently $384.5 million. In December 2012 the Company issued $150.0 million in private placement notes. This new debt was issued at an average rate of 3.2% and replaces $133.5 million in maturing debt with an average rate of 6.1%. Questar Corporation typically does not issue debt at the parent-company level. The parent instead issues debt at the subsidiary level, primarily to provide capital-structure clarity for regulatory purposes.[3] Of special mention is the note payable to Questar Corporation. Short term notes payable to the parent company have varied widely from the low of $87.0 million in 2009 to $166.1 million as of December 2012. As of June 30, 2013, the note payable has been reduced to $140.7 million. It appears that Questar Gas continues to use its parent company as a "bank" from which it obtains short-term loans according to its need for liquidity.

Page 5 of Exhibit 1 includes the operating statistics and looks at the revenue by customer class and the natural gas costs per Dth for each year under review. Residential and commercial sales provided 91.44% of the total revenue dollars but represented 59.05% of the total volume in 2012. Residential and commercial sales represented 93.43% of the revenue and 68.27% of the volume

[3] Questar Comments on Moody's Rating,, http://prnwire.com/cgi-bin/stories.pl?ACCT=104&STORY=/www/story/11-12-2002/0001839749&EDATE= > < Accessed June 9, 2010

for the first six months of 2013. Natural gas cost per Dth shows a slight decrease from $5.05 in 2011 to $4.77 in 2012. Natural gas cost per Dth for the first half of 2013 were not reported in the most recent SEC 10-Q filing.

Questar Corporation owns 100% of the stock in Questar Gas; therefore, the entire dividend payment of $8.875 million will be paid to Questar Corporation. The Company paid a total of $33.0 million in dividends during 2012 compared to $30.3 million in 2011. The $2.7 million increase represents an 8.9% growth rate compared to the historical average increase of 4.1%. The dividend payment represents a significant cash requirement for the Company and could become an issue if there is a downward trend in the overall profitability. At the present time, Questar Gas has adequate cash flow to maintain its debt service obligations and meet its financial needs. The Company is projected to maintain profitability levels similar to historical results and the Division will continue to monitor the actual results and the regulated return on equity.

On May 1, 2012, Questar Gas Company filed a legal action against QEP Field Services Company, a subsidiary of QEP Resources, Inc. The case, entitled *Questar Gas Company v. QEP Field Services Company*, was filed in the Third District Court in Salt Lake County, Utah. Questar Gas believes certain charges of QEP Field Services Company for gathering services exceed the amounts contemplated under a Gas Gathering Agreement, effective September 1, 1993, pertaining to certain gas produced by Wexpro Company under the Wexpro Agreement. Questar Gas is alleging breach of contract by QEP Field Services Company and is seeking an accounting and a declaratory judgment relating to the charges under the Gas Gathering Agreement. Since this issue has not been resolved, management cannot determine whether this litigation may have an adverse material effect on its financial position, results of operations or cash flows.

IV. CONCLUSION

The Division concludes that the payment of an $8,875,000 common stock dividend declared by Questar Gas's Board of Directors is within the discretion of the Company and it appears that there will be no impairment of the capital or the services rendered by the Company.

cc: Barrie McKay – Questar Gas

Michele Beck – Office of Consumer Services