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: June 24, 2015

RE: Questar Gas Dividend Declaration May 27, 2015
Docket No. 15-999-02

I. RECOMMENDATION – No Action

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

II. ISSUE

On May 27, 2015, the Board of Directors of the Company declared a quarterly cash dividend of $9.5 million. The dividend is payable to the Company's sole shareholder, Questar Corporation, on June 29, 2015. As required, the dividend declaration notice was published in the newspaper on June 2, 2015.

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 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, 2014, quarterly financial statements as of March 31, 2015, Questar Corporation News Release dated May 29, 2015, and a review of the Company's bond rating from the various bond rating agencies. The financial characteristics of Questar Gas generally indicate a profitable and stable utility company.

Exhibit 1 is a summary of the financial results for the periods ending December 31, 2009 through March 31, 2015. Because of the seasonal nature of the business, Questar Gas typically reports income in the 1st and 4th quarters of the year. For the 12 months ending December 31, 2014, total revenue saw a slight decrease of 2.53% from $985.8 million to $960.9 million. The decrease in total revenue is primarily driven by a decrease in the total volume and the price of the natural gas commodity due to warmer than normal weather conditions. In 2014, the weather was 17% warmer than normal. From a longer term perspective, total revenue has increased slightly from 2009 through 2014 with an average annual increase of 0.88%.

For the first quarter of 2015, total revenue was $21.5 million lower and the cost of natural gas sold was $21.0 million lower than the same period in 2014. The decrease in total revenue was the result of warmer than normal temperatures. Weather, as measured in degree days was 24% warmer than normal during the first quarter of 2015. While total revenue and gas costs were down, net income was $4.2 million higher than the same period last year. Effective March 1, 2014, Questar Gas received approval to increase rates as a result of a general rate case. The first quarter of 2015 represents the first full year that the new rates have been in effect.

Natural gas provided by Wexpro represented 62% of the natural gas supply in 2014 compared to 59% in 2013. For the first quarter of 2015, Wexpro production was 19% lower than the first quarter of 2014. The decline in production is a result of a slow-down in drilling and well completions due to the lower market price of natural gas. With a slow-down in the Wexpro production, the Company will be able to purchase additional gas supplies from outside supply sources. The current market price for natural gas is lower than the cost-of-service production gas from Wexpro.

The balance sheet information on pages 2 and 8 of Exhibit 1 identifies a slight decrease in accounts receivable from $209.9 million in 2013 to $205.3 million in 2014 and is down to $179.0 as of March 2015. The net plant and equipment has increased steadily from 2009 through 2014 averaging an 8.79% annual increase compared to total assets which increased at an average rate of 8.02%. Capital expenditures increased from $82.6 million in 2009 to $174.7 million in 2014 primarily due to the ongoing feeder line replacement program.

Page 4 of Exhibit 1 calculates the financial ratios for the periods under review. Short-term liquidity ratios for 2014 were higher than historical averages with the current ratio at 1.00 and the quick ratio at 0.61 compared to the average of 0.86 and 0.56. The profitability ratios are changing with the increase in capital expenditures in recent years. Return on Total Capital went down to 6.52% in 2014 compared to the average of 7.45%.

On an SEC financial reporting basis, the Company had a Return on Equity (ROE) of 9.41% for 2014. The Company’s authorized return on equity at the end of 2014 was 9.85% and is calculated based on different regulatory guidelines. The regulatory ROE is provided by the Company in the year-end Results of Operation and were calculated to be 9.53% for 2014. Based on the calculations, the Company does not appear to be earning more than the authorized rate of return.

On January 31, 2014, Moody's Investor Services upgraded Questar Gas and Questar Corporation from A3 to A2. Included in the Other Financial Indicators section on page 4 are calculations used by Moody's as part of its 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 by the rating agency as of year-end 2014.

The Company's regulatory capital structure for 2014 was 47.2% debt and 52.8% equity which is close to the historical average of 47.0% debt and 53.0% equity. Common equity grew at an average rate of 8.4% for the periods under review and included a $20 million equity contribution from the parent company in 2011.

Page 5 of Exhibit 1 includes the operating statistics and looks at the revenue by customer class along with the natural gas costs per dekatherm (Dth) for each year under review. Residential and commercial sales provided 91.1% of the total revenue dollars but represented 53.4% of the total volume in 2014. The volume of gas delivered to transportation and industrial customers represented 46.6% of the total volume in 2014 compared to the average of 39.3%. System natural gas cost increased to $5.98 per Dth in 2014 compared to $5.00 per Dth in 2013.

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.

On October 19, 2014, QEP Field Service and Tesoro Logistics LP (Tesoro) entered into a purchase agreement to transfer the related assets and liabilities of QEP Field Services to Tesoro. The purchase transaction was closed on December 2, 2014. On December 2, 2014, the court issued a memorandum decision granting two motions for partial summary judgement for breach of contract filed by Questar Gas. The court found that QEP breached the Gas Gathering Agreement by overcharging Questar Gas in its gathering rates. The court also denied two motions for partial summary judgement filed by QEP and denied cross-motions related to another claim. Due to the extended court proceeding, these issues may not be resolved for some time. 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.

Questar Corporation owns 100% of the stock in Questar Gas; therefore, the entire dividend payment of $9.5 million will be paid to Questar Corporation. 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.

IV. CONCLUSION

The Division concludes that the payment of a $9.5 million 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