

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

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

Docket No. 07-057-13

RATE OF RETURN REBUTTAL TESTIMONY OF JOHN J. REED

FOR QUESTAR GAS COMPANY

April 28, 2008

QGC Exhibit 4.0R

1 **Q. Are you the same John J. Reed who previously filed Direct Testimony in this**
2 **proceeding?**

3 A. Yes, I am. I provided Direct Testimony on behalf of Questar Gas Company
4 (Questar Gas or the Company). Please state the purpose of your Rebuttal
5 Testimony.

6 A. The purpose of my Rebuttal Testimony is to address the comments and
7 conclusions of Witness Charles E. Peterson from the Division of Public Utilities
8 (“Division”) regarding my testimony.

9 **Q. Have you revised your position regarding Questar Gas’ performance or the**
10 **appropriate ROE for Questar Gas?**

11 A. No, I have not.

12 **Q. Please provide a summary of your Rebuttal Testimony.**

13 A. Generally, I accept that Mr. Peterson’s additional financial metrics indicate that
14 Questar has enjoyed only average to below average financial performance.
15 However, I find that those data merely underscore my position, rather than refute
16 it. He does not challenge my findings regarding Questar Gas’s operational
17 performance or the savings that ratepayers have enjoyed as a result of that
18 performance.

19 **Q. Do you agree with Mr. Peterson’s assertion on page 42 of his testimony**
20 **regarding financial ratios that “Questar Gas is very much an average**
21 **company within this group of comparables”?**

22 A. For the most part, I do, given that Mr. Peterson is focused on financial ratios. In
23 fact, I find that supplemental information Mr. Peterson provides regarding other
24 gas distribution companies (Exhibit DPU 2.15) highlights Questar Gas’s average
25 to below average earnings levels. Questar Gas’s return on equity (ROE) was
26 lower than 8 out of 10 of the companies he reviewed. Specifically, Mr. Peterson’s
27 data indicate that for the period from 2001 to 2007, Questar’s Gas’ average ROE
28 was 9.9% compared with 14.93% for the two companies Mr. Peterson considered

29 the two “most pure natural gas distribution companies that are publically traded.”¹
30 Questar Gas was also significantly lower than the 12.58% mean ROE for his
31 entire group over that same period.

32 With regard to comparative statistics, my testimony is focused on providing
33 operational metrics that reflect Questar Gas’s efficiency and the customer benefits
34 derived from its superior performance. These measures, for the most part, are
35 simply different from the financial ratios reviewed by Mr, Peterson. They are not
36 in conflict.

37 **Q. Do you agree with Mr. Peterson’s position that his data do not “imply in any**
38 **way that Questar Gas deserves a premium cost of equity”²?**

39 A. I do not. Mr. Peterson’s data indicate that Questar does not enjoy even average
40 returns within the group of companies that he reviewed. His data further support
41 the notion that Questar Gas’s return on equity can be higher and still be within
42 industry norms. I continue to believe that setting Questar Gas’s ROE at the
43 higher end of the range being proposed by Mr. Hevert would be reasonable and
44 that any ratepayer impact from that higher ROE has already been more than off-
45 set by the Company’s superior performance.

46 **Q. What is Mr. Peterson’s ultimate conclusion regarding the link between**
47 **Questar Gas’s relative operational performance and the appropriate allowed**
48 **return on equity for the Company?**

49 A. Mr. Peterson concludes:

50 With this analysis the Company is seeking a reward for doing what
51 it is expected to do anyway. On that basis I would reject the
52 request. I would further reject the request because there is no
53 evidence that the financial markets would reward the Company
54 based on this analysis. Therefore, I conclude and recommend that

¹ Testimony of Charles E. Peterson, March 31, 2008, page 42 lines 925-926.

² Ibid, page 43, lines 936-938.

55 Questar Gas should not be rewarded with a premium cost of
56 equity.³

57 **Q. Do you differ with his conclusion?**

58 A. Yes, I fundamentally disagree with his conclusion. First, Mr. Peterson seems to
59 oppose linking earnings and management performance because he views it as a
60 form of incentive regulation, which he appears to oppose. Linking higher
61 earnings with better operational performance is exactly what would happen to an
62 unregulated firm, and we need to remember that a fundamental purpose of
63 regulation is to produce results similar to those that would be achieved in markets
64 where competition and free market forces are able to work. This is why many
65 state regulators incorporate a “management performance” element to setting the
66 appropriate return.

67 Mr. Peterson is correct that operational excellence, which produces
68 significant cost savings, is not likely to earn Questar Gas a reward from
69 the financial markets. That is because all of these savings ultimately
70 accrue to the benefit of ratepayers. Financial markets are focused on the
71 earnings of the Company, not the savings that the Company is able to pass
72 on to ratepayers. That is precisely why the Commission should adopt a
73 higher than average return for Questar Gas. Ratepayers are the
74 beneficiaries of Questar Gas’ actions, and they should be more than
75 willing to reward this performance by funding this higher level of earnings
76 through a very small proportion of the savings that Questar Gas has
77 produced.

78 **Q. Does this conclude your rebuttal testimony?**

79 A. Yes, it does.

³ Ibid. page 43, lines 949-953.

State of Massachusetts)
) ss.
County of Middlesex County)

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

John J. Reed

SUBSCRIBED AND SWORN TO this ____ day of April, 2008.

Notary Public