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2 PUBLIC SERVICE COMMISSION
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4 TRANSCRIPT OF PROCEEDINGS
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6 EVIDENTIARY HEARING
7 December 11, 2017
8 Jefferson City, Missouri
9 Volume 17
10
11 In the Matter of Laclede)
12 Gas Company's Request to) File No. GR-2017-0215
13 Increase Its Revenue for)
14 Gas Service)
15
16 In the Matter of Laclede)
17 Gas Company d/b/a Missouri) File No. GR-2017-0216
18 Gas Energy's Request to)
19 Increase Its Revenues for)
20 Gas Service)
21
22
23 NANCY DIPPELL, Presiding
24 REGULATORY LAW JUDGE
25
26 DANIEL Y. HALL, Chairman,
27 WILLIAM KENNEY,
28 SCOTT T. RUPP,
29 COMMISSIONERS.
30
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1 P R O C E E D I N G S

2 (Whereupon, the hearing resumed at
3 9:00 a.m. CST.)

4 JUDGE DIPPELL: Let's go ahead and
5 get started. Let's go on the record.

6 Good morning.

7 HEARING PARTICIPANTS: Morning,
8 Judge.

9 JUDGE DIPPELL: It is Monday
10 morning, December 11th, 2017, and we're here to
11 continue the rate cases in GR-2017-0215 and
12 GR-2017-0216. And let's see. In the matter of
13 -- for preliminary matters, we had -- and Miss
14 Payne, is she in here?

15 Mr. Thompson, maybe you can answer. We
16 had an Exhibit No. 56 on Friday, which Ms. Payne
17 was going to review before making -- deciding if
18 she had any objections.

19 MR. THOMPSON: I'm sorry, Judge.
20 She hasn't communicated anything to me about
21 that.

22 JUDGE DIPPELL: Okay. We will hold
23 that until after our next break.

24 And then we had the filing of some
25 substitute surrebuttal testimony by Office of

1 Public Counsel. Do you know if that is -- am I
2 to understand that's just corrections in the
3 schedules and so forth?

4 MR. SMITH: Yeah. Are you referring
5 to Ms. Azad, I think?

6 JUDGE DIPPELL: Yes.

7 MR. SMITH: I believe so.

8 Mr. Williams, Nathan Williams had filed that,
9 and I can't speak to that specifically --

10 JUDGE DIPPELL: Okay.

11 MR. SMITH: -- but that's my
12 understanding.

13 JUDGE DIPPELL: All right. I guess
14 we'll deal with that when we get to that as
15 well.

16 We are ready to begin capital structure
17 and cost of capital issues, and we're going to
18 begin today with opening statements on those
19 issues. Can we start with the Company?

20 MR. FISCHER: Thank you, Judge. May
21 it please the Commission. Welcome back, and I
22 hope everyone had a good weekend. I am Jim
23 Fischer, and today Mike Pendergast and I will be
24 representing Spire Missouri on this particular
25 issue.

1 There are really four parts to the
2 issue. There's of course the traditional ROE
3 issue, the capital structure issue, which is a
4 very important issue in this case, the cost of
5 debt, and then also the question of whether
6 short-term debt should be included in the
7 capital structure.

8 All the major trends, all the economic
9 trends over the last couple of years have showed
10 substantial improvement. Economic growth has
11 accelerated, the unemployment rate has fallen, I
12 think, to 4.1 percent, which most people
13 consider full employment, the Fed has raised
14 interest rates on several occasions as -- and
15 has indicated an intention to continue to raise
16 interest rates in the future in light of the
17 improving economy.

18 The Commission should determine what
19 rate of return on equity will permit the Company
20 to continue to attract investors while
21 reflecting the concerns and interests of
22 consumers. Such a balancing exercise should
23 also be consistent with the ROEs recently
24 determined by other regulatory utility
25 commissions for comparable companies.

1 In this case, the Company requests an
2 ROE of 10.35 percent based on the analysis
3 conducted by our expert Pauline Ahern.
4 Ms. Ahern has served as a consultant for
5 investor-owned utilities and municipal utilities
6 for nearly 30 years and has testified as an
7 expert witness in over -- before 31 regulatory
8 commissions. Her extensive background and
9 experience, if you're interested, are summarized
10 on Appendix A of her direct testimony.

11 Since Spire Missouri is not publicly
12 traded, Ms. Ahern uses a proxy group of natural
13 gas companies with similar risk to Spire
14 Missouri to -- for insight into what should be
15 the appropriate rate of return on common equity.
16 She testified an ROE of 10 percent before
17 adjusting for flotation costs and the smaller
18 size of Spire Missouri, and 10.35 percent after
19 those adjustments is both reasonable and
20 conservative given the Company's greater
21 business risk relative to the natural gas proxy
22 group.

23 In the last natural gas case decided by
24 the Commission, the Commission authorized an ROE
25 for Liberty of 10.00 percent. By contrast,

1 Staff's witness, David Murray, testifies in the
2 current case that his analysis shows that the
3 actual market cost of equity for Spire Missouri
4 is in the range of 6.90 to 7.70 percent. The
5 evidence will indicate that this remarkably low
6 range is substantially below any return on
7 equity authorized by the State Commission in
8 more than 30 years.

9 Mr. Murray recognized that his cost of
10 equity is much lower than the average allowed
11 ROEs for gas utilities in the country on page 39
12 of the Staff's cost of service report. On the
13 next page of that report, he indicates that the
14 average allowed ROEs for gas utilities during
15 the first six months of 2017 was 9.5 percent.
16 More recent information will indicate that the
17 authorized returns in 2017 have now gone up to
18 about 9.89 percent.

19 Perhaps for this reason, he does not
20 recommend his extremely low range of 6.9 to
21 70.0, and instead recommends an a range of 9.0
22 to 9.5 percent. And now as I understand his
23 testimony, it essentially takes the ROE of
24 9.5 percent that was authorized to KCPL and
25 lowers it to 9.25 percent to account for his

1 perceived risk differential between natural gas
2 companies and vertically integrated electric
3 companies, but from our perspective, this
4 approach is essentially a rearview mirror
5 approach, looking back on the conditions in the
6 test year in the KCPL rate case and not using
7 the improved economic data to review the current
8 conditions for the year that the rates will be
9 going into effect, which of course will be 2018.

10 In other words, given the improving
11 economy and the increasing Fed interest rates,
12 the authorized ROE should be higher as
13 recommended by Ms. Ahern.

14 Mr. Michael Gorman is appearing on
15 behalf of the Office of Public Counsel and MIEC.
16 His recommended range is 8.9 percent to
17 9.4 percent without adjustment for flotation
18 costs or the business risk of a smaller-sized
19 utility.

20 As Ms. Ahern explains in her rebuttal
21 testimony, he has some flaws in his analysis and
22 does not correct for flotation costs and
23 business risk. With her corrections and
24 adjustments, Mr. Gorman's recommended ROE would
25 be 9.89 percent.

1 The Company's also sponsoring the
2 testimony of three additional witnesses besides
3 Ms. Ahern to discuss the appropriate capital
4 structure to be utilized in this case.

5 Steven Rasche is the executive vice
6 president and chief financial officer for Spire
7 Inc., Missouri -- Spire Missouri's parent
8 company. Robert Hevert is a partner in the
9 consulting firm of ScottMadden and is a
10 well-known expert, I think, to the Commission,
11 since he's appeared in a number of cases before
12 the Missouri Commission in recent years.
13 Finally, Glenn Buck is the director of
14 regulatory and finance for the Company.

15 These witnesses support the use of the
16 actual capital structure of the public utility
17 Spire Missouri, Inc. as of the true update of
18 September 30, 2017.

19 As reflected in the Company's statement
20 of position and the true-up testimony that
21 Mr. Buck filed, the actual capital structure for
22 Spire Missouri, Inc. as of the true-up date is
23 45.8 percent long-term debt and 54.2 percent
24 common equity. We would also use the public
25 utility's actual cost of debt for the cost of

1 debt in this case.

2 Now, for purposes of setting rates,
3 Staff -- Staff witness Murray has recommended
4 the use of the capital structure of the parent
5 Spire, Inc. instead of the capital structure of
6 the public utility Spire Missouri as we have
7 proposed.

8 Staff has also recommended the
9 inclusion of short-term debt in Spire, Inc.'s
10 capital structure. Staff's capital structure is
11 more highly leveraged with 45.56 percent common
12 equity, 47.9 percent long-term debt, and 6.47 --
13 I'm sorry -- 6.47 with short-term debt.

14 Public Counsel and MIEC witness Gorman
15 has recommended the use of Spire Missouri's
16 actual capital structure with a couple of
17 adjustments. He -- he recommends the removal of
18 \$210 million of goodwill associated with the
19 acquisition of Missouri Gas Energy.

20 The capital structure, from our
21 perspective, is a very important issue. I
22 believe it may be the largest issue from a
23 dollar standpoint in the case. Much has changed
24 at the parent company level since the previous
25 Laclede Gas Company rate cases in which the

1 consolidated gas -- consolidated capital
2 structure of the parent was used.

3 In the past the use of the consolidated
4 capital structure as compared to the utility
5 specific capital structure was really a nonissue
6 since the long-term assets and financing at the
7 holding company level almost entirely consisted
8 of a Laclede Gas Company.

9 In other words, in previous cases, the
10 earnings potential of the parent, the Laclede
11 Group, consisted overwhelming of the two
12 regulated Missouri gas utility companies.
13 Today, though, Spire, Inc. is a holding company
14 with five local distribution companies across
15 three states, each with their own unique
16 regulatory and operating environments. It has a
17 FERC regulated natural gas transmission pipeline
18 as well as a gas marketing company, a propane
19 pipeline, and other smaller nonregulated
20 operations.

21 While it may have been appropriate in
22 the past to use the parent company's
23 consolidated capital structure when it
24 essentially -- the parent had the -- only two
25 Missouri regulated local distribution companies,

1 that's really not the case today. Staff's
2 proposed capital structure should be rejected,
3 since it would result in Missouri customer rates
4 being influenced by the financings completely
5 unrelated to the Missouri utilities.

6 As I mentioned, now the parent owns
7 out-of-state public utilities like Spire
8 Alabama, which was formerly known as the Alabama
9 Gas Corporation or Alagasco and the former
10 subsidiaries of Energy South. The capital
11 structure of the parent also supports the
12 unregulated activities of Spire Marketing, an
13 unregulated subsidiary of the parent, and a
14 FERC-regulated pipeline operation.

15 Under Staff's approach, the debt of
16 these operations would be included in the
17 capital structures for the public utilities in
18 Missouri. In fact, the public utility Missouri
19 issues its own long-term debt, and it's approved
20 by the Missouri Public Service Commission. It
21 has its own bond rating, and none of the debt of
22 the out-of-state utilities are secured by the
23 assets of the Missouri public utilities. It's
24 therefore appropriate to use the actual capital
25 structure of the public utility Missouri as the

1 capital structure for rate-making purposes.

2 In addition, as Ms. Ahern demonstrates,
3 the actual capital structure of Missouri public
4 utility is consistent with the capital
5 structures of other regulated companies in her
6 natural gas proxy group. It's also quite
7 consistent with the capital structure that was
8 previously used by the Staff in Laclede's last
9 rate case.

10 With regard to the short-term debt
11 issue, it's the Company's position that such
12 short-term debt costs should not be included in
13 the capital structure because the average level
14 of construction work in progress and other
15 commission tariff short-term assets such as the
16 margin calls on the Company's multi-year hedging
17 program and deferred gas costs, those exceed the
18 average level of short-term debt outstanding
19 during the true-up period after we take into
20 account the long-term debt issue that recently
21 occurred. This is consistent with the
22 Commission's long-term practice of not using --
23 or not including short-term debt in major
24 utilities' capital structures.

25 And then turning briefly to Mr. Gorman,

1 Mr. Gorman uses the capital structure of the
2 public utility, but he makes two adjustments.
3 The first adjustment is he takes -- he adjusts
4 for the recent \$170 million of long-term debt
5 which was used to refinance the short-term debt.
6 The Company now has also reflected that
7 adjustment in its true-up testimony, and so I
8 don't think that's any longer an issue between
9 us.

10 The second adjustment, though, he
11 argues that the common equity balance should be
12 reduced by \$210 million to remove capital
13 supporting the goodwill. This unprecedented
14 adjustment should also be rejected. The
15 goodwill is related to the premium paid for
16 MGE's assets in excess of the net book value of
17 those assets.

18 The parties agreed in the acquisition
19 case that no portion of the goodwill balance
20 should be included in rates. In fact, the
21 goodwill balance in this case has been removed
22 or excluded from the Company's rate base.

23 The acquisition of MGE was funded by a
24 mix of capital, primarily long-term debt and
25 common equity. Unlike the implications of

1 Mr. Gorman's adjustment, the goodwill associated
2 with the purchase of MGE assets was not financed
3 entirely by common equity. But in any event,
4 it's not possible to trace specific portions of
5 the acquisition financing to specific assets,
6 including the goodwill as Mr. Gorman suggests.

7 For these reasons, we believe
8 Mr. Gorman's proposed adjustment should
9 rejected.

10 Now, during the opening statement at
11 the beginning of this case, Miss Shemwell showed
12 you a chart of how Laclede's stock price has
13 gone up over the years, and I'd like to show you
14 a similar chart which shows you the -- also the
15 performance during that five-year period of the
16 Standard & Poors 500, which shows that our Spire
17 performance has been almost the same as the
18 Standard & Poors performance, and it also has
19 another line that shows you the performance of
20 peer groups in the natural gas peer group.
21 They've done actually better. They went up
22 101.7 percent. Spire's stock increased by
23 73.6 percent or about the same rate as the
24 Standard & Poors.

25 With that I would close and take any

1 questions. Our experts are here to answer your
2 technical questions.

3 JUDGE DIPPELL: Commissioners, do
4 you have questions for Mr. Fischer?

5 CHAIRMAN HALL: Yeah.

6 Could you explain to me why I should
7 care about that? Why --

8 MR. FISCHER: You know, I know we
9 talk about stock price as part of the ROE
10 adjustments, and I think it's just important, if
11 we're going to look at how much the stocks of
12 utilities have gone up over a period, we need to
13 also note that the market as a whole has gone up
14 substantially during that period, but that's
15 primarily. I don't think it's as important as
16 folks might make it out to be.

17 CHAIRMAN HALL: But you think it is
18 important, not just --

19 MR. FISCHER: I think if you're
20 going to look at what our stock has done over
21 five years --

22 CHAIRMAN HALL: Should we? Should
23 we be looking at what your stock has done over
24 the last five years?

25 MR. FISCHER: I think when you look

1 at things like yield, you do take into account
2 the stock price, but I think it's important to
3 understand all the economic condition, including
4 the rising stock market.

5 JUDGE DIPPELL: I believe that's all
6 the Commission questions.

7 Do we have an opening from Staff?

8 MR. THOMPSON: Thank you, Judge.

9 JUDGE DIPPELL: You're going to save
10 me from not being able to get it back to the
11 camera.

12 MR. THOMPSON: That chart simply
13 depicts the positions of the parties if the four
14 cost of capital issues.

15 May it please the Commission?

16 JUDGE DIPPELL: Go right ahead.

17 MR. THOMPSON: Four issues in the
18 area of cost of capital. The first one, return
19 on equity. The task of the return on equity
20 witness in a case of this kind is to determine
21 what an investor, what return an investor would
22 have to have to invest in this security as
23 opposed to another investment opportunity of
24 similar risk.

25 So Staff has suggested a range of 9.0

1 to 9.5. Mr. Gorman, on behalf of OPC, MIEC, and
2 I think NICG has suggested a range of 8.9 to
3 9.4, and the Company suggests 10.35. That is
4 not the highest -- that does not exceed the
5 highest awarded ROE for the past year, but it's
6 quite close, it's quite close. It's well above
7 the average, and so you would have to ask
8 yourself is this company so affected with risk
9 that an investor would have to have a return of
10 10.35 percent in order to choose this investment
11 over the other opportunities in the market. I
12 mean, of course an investor would like a return
13 of 10.35, but as Mr. Fischer told you,
14 Mr. Murray's analysis shows that investors are
15 actually buying this stock with a return of 6.9
16 to 7.7.

17 So there is simply nothing but air in
18 that 10.35, and as Mr. Gorman and Mr. Murray
19 have testified, or I guess we should say will
20 testify when you receive their pre-filed
21 testimony, you will see that Ms. Ahern has
22 adopted a number of different devices in order
23 to inflate that number. Staff suggests that is
24 an inflated number, you should not rely on it,
25 you should not adopt it.

1 Capital structure. Traditionally with
2 this company, the Commission has used the
3 consolidated capital structure of the holding
4 company, formerly the Laclede Group, now Spire.
5 Things have changed. It's true. The Laclede
6 Group, now Spire, owns several more operating
7 companies than it used to. That's true. But
8 Spire Missouri continues to be its main
9 operating company, the largest and most
10 lucrative of those operating companies.

11 Staff continues to believe that the
12 consolidated capital structure of the parent is
13 the appropriate capital structure for
14 rate-making purposes.

15 Number one, it's the capital structure
16 that investors can actually invest in. No one
17 can buy stock of Spire Missouri. That stock is
18 all owned by the holding company. So if you
19 want to invest in Spire, you're investing the
20 holding company.

21 Number two, there's that pesky goodwill
22 that Mr. Gorman talks about. If Missouri
23 ratepayers are going to pay the capital costs of
24 the goodwill, which is to say the acquisition
25 premium that this company paid when it purchased

1 Alagasco -- or excuse me -- I guess in this case
2 when it purchased MGE, then that is an indirect
3 recovery of the acquisition premium, which this
4 company agreed it would never seek from Missouri
5 ratepayers.

6 So if you decide to make rates with
7 Spire Missouri's capital structure, then I
8 suggest you make the adjustment that Mr. Gorman
9 has suggested and remove that amount from the
10 capital structure.

11 Cost of long-term debt, Staff and OPC
12 are agreed at 4.159, here rounded to 4.16, and
13 Staff alone of the parties urges the inclusion
14 of the amount of short-term debt. The reason is
15 the short-term debt represents the carrying
16 costs of the gas and propane inventory, and it's
17 unusual for Staff to propose a short-term debt
18 be included, but this is an unusual situation.

19 How that short-term -- how the gas
20 inventory and propane inventory are going to be
21 handled is in fact an issue in this case that
22 you will be taking up later on. Thank you very
23 much. Be happy to answer questions.

24 JUDGE DIPPELL: Any questions for
25 Mr. Thompson?

1 CHAIRMAN HALL: No questions. Thank
2 you.

3 JUDGE DIPPELL: Thank you,
4 Mr. Thompson.

5 MR. THOMPSON: Thank you, Judge.

6 JUDGE DIPPELL: Public Counsel.

7 MR. SMITH: Morning. My name is
8 Ryan Smith with the Office of the Public
9 Counsel. May it please the Commission?

10 JUDGE DIPPELL: Go ahead, Mr. Smith.

11 MR. SMITH: The topic of this issue
12 is capital structure and the costs of capital
13 which gets at the heart of OPC's overearnings
14 complaint. The Company has requested in this
15 case an equity-rich capital structure at a high
16 return on equity. Before I get into my comments
17 on that, I would like to address something that
18 counsel for Spire, Mr. Rick Zucker, stated in
19 his opening at the beginning of this case on
20 this topic.

21 The start of this case, counsel accused
22 Staff, Office of the Public Counsel and
23 presumably many other parties of wanting to
24 "misappropriate" millions of dollars that
25 "rightfully belong" to the companies.

1 Words like "misappropriate millions of
2 dollars" and "rightfully belong to the
3 companies" may sound good to the shareholders,
4 but these words take on a different meaning when
5 we have customers in this state who cannot
6 afford gas bills. OPC represents those
7 customers. They are of all types, retired,
8 fixed income, young families struggling to make
9 ends meet.

10 OPC first raised concerns about
11 excessive profits by this company in April
12 of 2016, when OPC observed facts corroborating
13 the theory that the Company was making excessive
14 profits, and the facts that they observed came
15 in part from these quarterly surveillance
16 reports.

17 You will hear later today about these
18 quarterly surveillance reports. In fact, the
19 Company is resisting the invitation to enrich
20 the transparency of its surveillance --
21 surveillance reports which will be a litigated
22 topic on today's docket.

23 OPC is working with MIEC to explore
24 these earnings issues. OPC and MIEC's position
25 on capital structure and cost of capital are

1 jointly sponsored by Mr. Michael Gorman. He'll
2 be available for any questions about his
3 methodologies, about his recommendations. He
4 has testified many times before this Commission
5 and others. He's highly skilled, highly
6 experienced, highly credible.

7 Through Mr. Gorman's analysis, OPC
8 points out about the capital structure issue,
9 that common equity is the most expensive kind of
10 capital. In fact, common equity is more than
11 twice as expensive as debt capital. And the
12 utility is requesting a capital structure that
13 is equity rich. The capital structure, too
14 heavily weighted with common equity, will
15 unnecessarily increase the burden on ratepayers.

16 OPC and Staff are in agreement that the
17 Company's proposed capital structure of 54.2
18 percent common equity to 45.8 percent long-term
19 debt is weighted too heavily with common equity.
20 Compare the 54.2 percent of the Company with
21 Mr. Gorman's number of 47.2 percent equity, and
22 Staff witness, Mr. David Murray's common equity
23 structure of 45.6 percent equity.

24 Staff and OPC's structures are more in
25 line with a reasonable and a prudent capital

1 structure, and one that met more closer -- more
2 close than matches the utility's peers. The
3 Company has also unreasonably included a premium
4 payment for the purchase of MGE or goodwill in
5 its capital structure as a part of his capital
6 structure proposal. Mr. Gorman can discuss
7 further why it is inappropriate to make that
8 adjustment.

9 Now, Staff capital structure is a
10 little bit different than OPC's in the sense
11 that it included a short-term debt rate for gas
12 inventory carrying costs. The reason OPC's
13 capital structure does not contain a short-term
14 debt rate is that OPC is recommending that that
15 short-term debt rate be recovered through the
16 PGA.

17 So if this Commission wanted to give
18 rate-based treatment to gas inventory, OPC
19 actually agrees that some amount of short-term
20 debt would need to be included, and actually,
21 Staff witness Mr. Murray recommended a path to
22 accomplish that objective at pages 38 and 39 of
23 the surrebuttal testimony.

24 Staff and OPC/MIEC developed similar
25 returns on common equity with Staff at 9.25 and

1 OPC at 9.2. It has already been discussed that
2 the Company is proposing a 10.35 inflated return
3 on equity. OPC would ask this Commission in
4 closing that it order a prudent, reasonable
5 capital structure that's not overweighted with
6 equity and provides a just and a reasonable
7 return that's no higher than the 9.4 percent
8 recommended by Mr. Gorman. Thank you.

9 JUDGE DIPPELL: Are there any
10 questions for Mr. Smith?

11 CHAIRMAN HALL: No questions.

12 JUDGE DIPPELL: Thank you.

13 All right. Is there anything from
14 Division of Energy?

15 (No response.)

16 JUDGE DIPPELL: Not here today.
17 Environmental Defense Fund?

18 MS. KARAS: Nothing, your Honor.

19 JUDGE DIPPELL: Midwest Energy
20 Consumers.

21 MR. WOODSMALL: Thank you. I'll be
22 very brief.

23 One of the benefits of going later is a
24 lot of times your comments are already taken,
25 and I applaud Mr. Smith on behalf of Public

1 Counsel. Many of his comments reflect the
2 positions that MECG takes. Similarly, Staff's
3 position on capital structure and ROE, I think,
4 are similar with MECG.

5 MECG's position is that you need to set
6 a capital structure that recognizes the low cost
7 of debt. You don't want to put too much debt in
8 because it makes the Company too risky, but
9 there needs to be an appropriate amount of debt.
10 Staff and Public Counsel both get there in
11 different ways. Staff says use the consolidated
12 capital structure, and it makes a lot of sense.
13 You do that in a lot of other cases. You just
14 did it in KCP&L's case. And the theory there,
15 as Mr. Thompson said is, the consolidated
16 capital structure, that is the only company that
17 investors can truly invest in. So it makes
18 sense to use a consolidated capital structure as
19 you've done many, many times over.

20 The other alternative that gets to
21 similar position is what Mr. Smith told you is
22 sponsored by Mr. Gorman. And that is if you use
23 the assigned capital structure for Laclede/MGE,
24 take out the goodwill.

25 Now, the companies would have you

1 believe this is an unprecedented adjustment, and
2 to some extent, it is unprecedented, but that's
3 because no other company faces this. If you
4 think about when Great Plains was going to buy
5 Westar the first time around, when it failed,
6 they agreed, as part of their initial filing, to
7 book all goodwill at the parent company level.
8 Similarly, when Great Plains bought GMO, all
9 goodwill was booked at the parent company level,
10 so there was no need for this type of
11 adjustment. Only here, where the Company didn't
12 book this goodwill at the parent company level
13 is an adjustment necessary. So it's only
14 unprecedented because the other utilities don't
15 book the goodwill at the subsidiary level.

16 So capital structure, we agree with
17 either Public Counsel or Staff both lead to a
18 reasonable capital structure. On ROE, Staff and
19 Public Counsel get to the same point virtually.

20 A couple comments I wanted to make on
21 the Company's capital ROE. The Company does an
22 analysis and comes up with an ROE of 10.00, but
23 then the Company adds 35 basis points
24 through 2 adders. The first one is a size
25 adder. The theory is that Laclede and MGE --

1 I'm not talking Spire -- Laclede and MGE are so
2 small that they have additional risk, but that
3 ignores the fact that Spire exists. That
4 ignores the fact that Laclede and MGE have a
5 shared services agreement with Spire.

6 So Laclede and MGE don't have the risk.
7 They turn to Spire for legal services and IT
8 services and capital access and for management
9 services. So the risk of a smaller company
10 doesn't exist. In fact, Spire allocates those
11 costs, and they recover it through rates from
12 Laclede and MGE ratepayers.

13 So the size adder doesn't make sense.
14 The other adder, and Mr. Gorman can talk more
15 about this, regards flotation costs. Flotation
16 costs are the costs that you incur when you
17 access the equity markets, the cost to issue
18 stock.

19 Ms. Ahern says that she estimates that
20 the Company's would have -- Laclede and MGE
21 would have had you issue stock and incur -- I
22 think it was \$56 million of flotation costs.
23 Mr. Gorman's primary position on that is well,
24 that assumes that everything that they needed
25 would have been done through equity infusion and

1 ignores the fact that they would have retained a
2 bunch of earnings.

3 So both of those adders are misplaced,
4 as Mr. Gorman says, and MECG supports that
5 position.

6 JUDGE DIPPELL: Any questions for
7 MIEC?

8 CHAIRMAN HALL: No questions.

9 JUDGE DIPPELL: Thank you,
10 Mr. Woodsmall.

11 MIEC.

12 MR. MILLS: Good morning. May it
13 please the Commission.

14 The first thing I want to talk about is
15 the capital structure issue, and the one thing
16 that I would like you to take away from my
17 opening statement is that a rate adjustment to
18 correct a capital structure that is not in the
19 public interest is just like any other
20 rate-making adjustment. This is not a
21 particular area that requires the Commission to
22 keep its hands off.

23 So if the utility has chosen to reflect
24 on its books a capital structure that is
25 unreasonably costly to ratepayers, the

1 Commission should order an adjustment for
2 rate-making purposes. It's that simple. This
3 is no different than adjustments to remove
4 unnecessary, unreasonable expense like luxury
5 boxes or an adjustment to disallow a certain
6 level of incentive compensation that doesn't
7 benefit customers.

8 Now, it's a truism and to an extent, it
9 is true that you should not substitute your
10 judgment for that of the Company's management,
11 but for regulation, to have any effect at all,
12 you must make rate-making adjustments when the
13 utility has chosen a path that rewards
14 shareholders and harms ratepayers.

15 So back to my analogy of the luxury
16 boxes, if you believe that a utility's
17 expenditures on luxury boxes at a stadium is not
18 an expense that benefits ratepayers, you make --
19 you make an adjustment and disallow that expense
20 for rate-making purposes. It's pretty simple.
21 It's done all the time.

22 Does that mean that the utility can't
23 continue to spend money to keep its luxury box?
24 Of course not. It just means it can't make the
25 ratepayers cover that expense, because you have

1 decided it's been reasonable.

2 Now, think about executive
3 compensation. If the utility is paying its
4 C-suite three times more than any other
5 regulated utility and if there's good evidence
6 that such compensation does not benefit
7 ratepayers, you would disallow some level of
8 that compensation, and you would set rates based
9 on reasonable level of compensation. That
10 doesn't mean you're limiting how much executives
11 are paid.

12 If shareholders think the executives
13 are worthy, they can certainly continue that
14 level of pay, but you would have done your job
15 of determining what level of cost is reasonable
16 for ratepayers to bear, and after all, that's
17 the whole point of rate cases. For all the
18 issues that you're hearing, there's very little
19 dispute over actual expenditures. What the
20 utilities actually spent in the test here is
21 rarely an issue, and it's not an issue in this
22 case on capital structure. We can easily
23 reconcile the rate-making impact of a
24 commissioned decision that establishes a
25 reasonable level of capital -- a reasonable

1 level of equity in the Company's capital
2 structure.

3 And just like any other rate-making
4 adjustment, by ordering that rates be set on the
5 basis of a reasonable capital structure, you are
6 not requiring the Company to issue more debt, to
7 issue more equity or retire any debt. Just like
8 with luxury boxes or promotional advertising or
9 executive compensation, if you order an
10 adjustment for rate-making purposes, you're not
11 ordering the utility to take any particular
12 action. If you disallow the luxury box expense,
13 they can keep paying it. That's a decision that
14 management and shareholders need to come to.

15 So management may very well decide that
16 it is -- that is not in the best interest to
17 continue to pay for things like an equity-rich
18 capital structure or luxury boxes or excessive
19 executive compensation, and if they -- if they
20 decide that they want to continue to pay those
21 expenses, then we'll have to find some way to
22 cut costs in other areas to cover them.

23 So it's the same thing with capital
24 structure. If you determine, and you should,
25 that the Company has chosen to finance its

1 operations with too much expensive equity and
2 too little cheap debt, you make a rate-making
3 adjustment. That doesn't mean that you're
4 ordering the Company to buy back stock or issue
5 more debt. They can continue to maintain
6 exactly the same capital structure as they -- as
7 they have proposed in this case. Such an
8 adjustment merely means that you've determined
9 that just like paying for a luxury box at a
10 stadium, that the Company has chosen a path that
11 harms ratepayers and excessively benefits
12 shareholders.

13 The other issue that's up for hearing
14 this morning is -- is return on equity, and as I
15 said in my general opening last week, ROE of
16 course is a very important issue, there's a lot
17 of dollars at stake there, and it certainly
18 is -- is an issue that you need to take
19 seriously, but frankly, it's a pretty routine
20 issue at this point.

21 The Commission in Missouri has awarded
22 electric utilities to regulate about a nine and
23 a half percent return, and they're going
24 gangbusters. They're increasing dividends,
25 their stock prices are climbing, they're

1 entering into mergers and acquisitions, and most
2 importantly, they're continuing to provide safe
3 and adequate service.

4 Now, there's no dispute that LDCs are
5 less risky than vertically integrated electric
6 companies, and a reasonable return for an LDC is
7 therefore lower than a reasonable return for a
8 vertically integrated electric company.

9 Now, from my point of view, you have
10 made reasonable decisions over the last few
11 years on return of equity. That's not to say
12 they shouldn't have been a little lower, but
13 they've been reasonable, and there's nothing in
14 this record in this case that I think would make
15 you want to abandon that path of awarding
16 reasonable rates of returns.

17 So if your electric companies are
18 flourishing at 9.5 percent, what earthly reason
19 is there to award this company a 10.35 percent?
20 There is none. Such a return would only benefit
21 shareholders.

22 Now, Mr. Gorman, who's jointly
23 sponsored by MIEC and OPC will be appearing
24 today. You've always -- you've always found
25 Mr. Gorman to be a reasonable witness, and he's

1 recommended an ROE of 9.2 percent. And given
2 what you've allowed other utilities and given
3 the debt and equity markets today, and given the
4 difference in risk profiles between vertically
5 integrated electric utilities and gas LDCs,
6 that's a very reasonable, even a comfortable
7 rate of return for Spire in this case.

8 And I urge you to take advantage of
9 Mr. Gorman's appearance today. He's not only a
10 preeminent expert on this topic, but he's very
11 approachable. He's not stuffy; he's not
12 pretentious. If you ask him a straight
13 question, he'll give you a straight answer, and
14 that's certainly something that you all can
15 benefit from today. Thank you.

16 JUDGE DIPPELL: Any questions for
17 Mr. Mills?

18 CHAIRMAN HALL: No questions.

19 JUDGE DIPPELL: Thank you.

20 Are there any other intervenors
21 present that would like to make an opening
22 statement?

23 (No response.)

24 JUDGE DIPPELL: Seeing none, all
25 right. With that then, I believe we are ready

1 to begin with our first witness by Spire.

2 MR. FISCHER: Yes, Judge. Spire
3 would call Pauline Ahern to the stand. We -- I
4 don't know, your -- your witness list may have a
5 different order, but we thought we'd put our ROE
6 up first and then take capital structure
7 altogether, if that's all right with you and the
8 parties.

9 JUDGE DIPPELL: That's fine here and
10 I'm not seeing any objections.

11 MR. FISCHER: Judge, just for
12 purposes of letting people know what we had in
13 mind too, after Ms. Ahern, we were going to put
14 Steve Rasche and then Robert Hevert and then
15 Glenn Buck on the stand, in that order.

16 JUDGE DIPPELL: All right.

17 (Witness sworn.)

18 THE WITNESS: I do.

19 JUDGE DIPPELL: Thank you.

20 Go ahead, Mr. Fischer.

21 MR. FISCHER: Thank you.

22

23 PAULINE M. AHERN testified as follows:

24 DIRECT EXAMINATION BY MR. FISCHER:

25 Q. Please state your name and address for

1 **the record.**

2 A. My name is Pauline M. Ahern, A-H-E-R-N.
3 My business address is -- not my mailing
4 address -- is 1900 West Park Road, Suite 250,
5 Westborough -- that's O-U-G-H -- Mass,
6 Massachusetts, 01581.

7 My mailing address is 3000 Atrium Way,
8 Suite 241, Mt. Laurel -- two words -- New
9 Jersey, 08054.

10 Q. Are you the same Pauline Ahern that
11 caused to be filed in this proceeding Direct
12 testimony which has been marked as Exhibit
13 No. 38; Rebuttal that's been marked as 39;
14 public version of a Surrebuttal which has been
15 marked 40; and a confidential version of that
16 Surrebuttal has been marked as Exhibit 41?

17 A. Yes, I am.

18 Q. Do you have any changes or corrections
19 that need to be made to any of those exhibits?

20 A. I have a few, about six.

21 Q. Okay.

22 A. The first one is in the direct
23 Exhibit 38, page 25, lines 18 and 19, the phrase
24 after the word "DCF, comma," it reads: "The
25 recent dramatic rise in interest rates in

1 response to recent Federal Reserve comments."
2 Should be deleted.

3 **Q. And do you have another change?**

4 A. Not in the direct, no.

5 The next is in the rebuttal, Exhibit 39
6 on page 20 -- I'm sorry -- page 30, footnote 38
7 should read all caps: SBBI-2017, underlined, at
8 10-22. And that document was provided as part
9 of the work papers to the rebuttal.

10 JUDGE DIPPELL: Can you repeat that?

11 THE WITNESS: Footnote 38 should
12 read: SBBI, all caps, hyphen, 2017. That
13 should be all underlined, at 10-22.

14 And the last changes are in the
15 surrebuttal, my surrebuttal. All I have here is
16 the proprietary Exhibit 41. On page 5, line 26.

17 BY MR. FISCHER:

18 **Q. Is any of this confidential?**

19 A. No. It -- I don't believe so. I'll
20 double check. (Reviewing document.)

21 No.

22 **Q. Okay. Go ahead then.**

23 A. Okay. Page 5, line 26, the fourth word
24 from the right margin is "appear." It should be
25 plural, "appears." Oh, one is just a quotation

1 that would go in the confidential. I won't read
2 that one in. Is that all right?

3 **Q. Yes.**

4 A. Page 39. I mean a quotation mark not a
5 quotation. Page 39, line 11. One, two, three,
6 four, five, six... seven -- seven words from the
7 right, there's the phrase "that is an RSM." It
8 should read "that if an RSM."

9 **Q. Do you have anything else that needs to**
10 **be corrected?**

11 A. No, I don't.

12 **Q. And if I ask you the same questions**
13 **that are contained in your testimony today,**
14 **would your answers be the same and true and**
15 **accurate to the best of your knowledge and**
16 **belief?**

17 A. Yes, they would.

18 MR. FISCHER: Judge, then I think
19 this is the only set of issues that Pauline will
20 be appearing on -- in this case on, and I would
21 ask for the admission of Exhibits 38, 39, 40 and
22 41 and then tender her for Cross. Before I do,
23 though, I should also -- I think I misspoke.
24 Mr. Hevert will follow her in the order.

25 JUDGE DIPPELL: All right.

1 Would there be any objections to
2 Exhibits 38, 39, 40 and 41?

3 (No response.)

4 JUDGE DIPPELL: Seeing no objection,
5 I will admit those into evidence.

6 (SPIRE EXHIBITS NOS. 38, 39, 40 AND
7 41 RECEIVED INTO EVIDENCE.)

8 JUDGE DIPPELL: And we can begin
9 Cross-Examination with Staff.

10 MR. THOMPSON: Thank you, Judge.

11 JUDGE DIPPELL: Oh, and I'll just
12 interrupt briefly. Since we do have
13 confidential testimony, I'll expect the
14 attorneys to help me police that if something in
15 the -- and the witness, for that matter, if you
16 know of something that you need to answer or
17 something that we need to go in camera, just let
18 me know.

19 THE WITNESS: Okay.

20 MR. THOMPSON: Thank you, Judge.

21 JUDGE DIPPELL: Thank you, Counsel.

22 CROSS-EXAMINATION BY MR. THOMPSON:

23 **Q. Good morning, Ms. Ahern.**

24 A. Good morning.

25 **Q. You're employed, I believe you said,**

1 with ScottMadden?

2 A. Correct.

3 Q. And what is your hourly rate?

4 A. I believe on this particular project,
5 it -- it -- well, I know it's \$350.

6 Q. Do you know how many hours you have
7 devoted to this case so far?

8 A. No, I don't.

9 Q. Who would know that?

10 A. I would. I think it's in my time
11 sheet, but I don't -- I have not added them all
12 up.

13 Q. Okay.

14 A. And all the hours would be on my
15 invoices that have been provided to the Company.

16 Q. Now, you're not the only employee of
17 ScottMadden that's participating in this case;
18 isn't that correct?

19 A. Correct.

20 Q. Who else is an employee of ScottMadden?

21 A. Mr. Robert Hevert.

22 Q. Mr. Hevert. And just you two?

23 A. As witnesses, yes.

24 Q. In other words, is there anyone --
25 okay. Thank you.

1 **And do you happen to know how much**
2 **ScottMadden has billed so far?**

3 A. No, I don't.

4 **Q. Okay.**

5 MR. THOMPSON: No further questions,
6 Judge. Thank you.

7 JUDGE DIPPELL: Thank you.
8 Public Counsel?

9 MR. SMITH: No questions.

10 JUDGE DIPPELL: MIEC?

11 MR. MILLS: Yes.

12 CROSS-EXAMINATION BY MR. MILLS:

13 **Q. To follow up on Mr. Thompson's**
14 **question, are there other employees of**
15 **ScottMadden that have done work on this case**
16 **that aren't appearing as witnesses?**

17 A. Yes. We have a team and, you know,
18 that we rely on. I'm not sure whether
19 Mr. Hevert relied on the team for his testimony.
20 I had analysts working on it with me and people
21 editing.

22 MR. MILLS: Thank you. That's all I
23 have.

24 JUDGE DIPPELL: Midwest Energy
25 Consumers?

1 MR. WOODSMALL: Yes.

2 CROSS-EXAMINATION BY MR. WOODSMALL:

3 Q. Very briefly, Mr. Thompson asked you
4 some compensation questions. Do you know how
5 much your budget is for this case?

6 A. No. And I'll tell you why. I
7 typically -- my fees typically run -- and I
8 don't know what it is for this particular case
9 on a here it is, ready-to-file basis for the
10 direct testimony, because that was a single
11 charge, and following the filing of direct
12 testimony, it's on an hourly basis. We don't
13 know how many witnesses there are going to be,
14 we don't know how many discovery requests there
15 are going to be, we don't know whether we need
16 to appear at hearings. Rarely am I asked for
17 can you give me -- except for tiny companies,
18 can you give me an estimate of what your
19 rebuttal costs might be or your presence at
20 hearings.

21 And to the extent I can, I utilize
22 people at, you know, support Staff, technical
23 Staff, analyst Staff, and then that reduces the
24 overall composite hourly rate, but there was no
25 budget, no -- I did not give a budget and said

1 this is the project cost.

2 **Q. So there is no ceiling in the amount**
3 **that you could have charged in this case?**

4 A. The technical answer is yes, unless I
5 had been involved in cases where if it exceeds a
6 certain amount, I can't go over that without
7 approval.

8 **Q. So what is the ceiling that --**

9 A. That was not specified in this case.

10 **Q. So there is a ceiling, but it wasn't**
11 **specified?**

12 A. It wasn't specified, but I can tell you
13 that on all the cases I've been in, the amount
14 of hours that have been spent have been rather
15 typical.

16 **Q. Can you tell me then how the ceiling**
17 **would be quantified if it wasn't specified?**

18 A. No. It's not -- it's not quantified in
19 this case. In other cases, the client has
20 specified a ceiling.

21 **Q. Okay. In this case, is there a**
22 **ceiling --**

23 A. No.

24 **Q. -- in the amount you could have**
25 **charged?**

1 A. No, there is not.

2 MR. WOODSMALL: Okay. Thank you.

3 JUDGE DIPPELL: Is there anything
4 from Environmental Defense Fund?

5 MS. KARAS: No questions, your
6 Honor.

7 JUDGE DIPPELL: Are there questions
8 from the Bench?

9 CHAIRMAN HALL: Yeah, I have a few.

10 QUESTIONS BY CHAIRMAN HALL:

11 Q. Good morning.

12 A. Good morning.

13 Q. What is the role of risk in a proper
14 determination of an ROE for a regulated utility?

15 A. The assessment of risk is essential in
16 the proper assessment or estimation of the
17 required return on equity because the required
18 return on equity is a function of investors'
19 expectations of risk.

20 When they put their money, when they
21 buy a common stock, they buy it with a required
22 return necessary to compensate them for whatever
23 risk they're taking on. So when they look at
24 one, two or three different investments, they
25 know they're -- you know, risk profile, how

1 much -- how risk averse they want to be or they
2 are, whether they want to invest in something
3 safe such as municipal bonds, or they want to go
4 into a riskier venture, utility stock, or an
5 even riskier venture, like Amazon or venture
6 capital project.

7 They assess their assessment of the
8 risk they're willing to take on and they look at
9 the opportunities they have to invest and what
10 would match their risk assessment, and they try
11 to maximize the return and put their money in an
12 investment where the required return is going to
13 match their risk assessment.

14 **Q. Generally, what is the relationship of**
15 **risk between vertically integrated electric**
16 **utilities and gas utilities?**

17 A. Generally, all else equal, vertically
18 integrated utilities, because they are in a
19 production process, are riskier than
20 transmission LDCs or electric transmission
21 companies, but the quantification of that risk
22 comes through looking at the market data --

23 **Q. Right.**

24 A. -- and advising -- you know, because
25 the market data represents the results of the

1 decisions that the investors are making based on
2 their perceptions of risk.

3 **Q. So if this Commission were to determine**
4 **that there was a particular appropriate ROE**
5 **based upon risk for an electric utility and in**
6 **the exact same time frame, was trying to make a**
7 **risk analysis so as to determine an ROE for a**
8 **gas company, the ROE for the gas company should**
9 **be lower?**

10 A. As I said earlier, all else equal.

11 **Q. Right. Well, that was inherent --**

12 A. Yeah, all else is not necessarily
13 equal.

14 **Q. That was inherent in the question.**

15 A. Okay. What I think is if you've got
16 two cases before you and one's an electric and
17 one's a gas, LDC, an integrated electric, you
18 really need to look at the evidence of the
19 individual records and see where it comes out,
20 because all -- all of the factors that the
21 investors take into account when making the
22 decisions will be reflected in the market data
23 and, therefore, should be reflected in the
24 estimations of the -- the regular -- the cost of
25 equity models that we use.

1 Q. So what's happened t -- and there's
2 been some discussion about this and some
3 testimony and evidence as well, but just to
4 recap, what -- what has happened to -- to
5 Spire's stock prices over the last five years?

6 A. They have risen. They have risen
7 significantly. They -- as the chart showed,
8 they have not risen as significantly as have
9 their peers.

10 Q. When you say that, "as their peers,"
11 explain that to me.

12 A. Well the peer group or the S&P 500 that
13 were on that chart and that's --

14 Q. Yeah, I couldn't see that chart. So --

15 A. Oh, okay.

16 Q. -- it didn't -- it didn't do much for
17 me.

18 A. Oh, okay.

19 MR. FISCHER: Would you like to have
20 something better to look at, Judge?

21 CHAIRMAN HALL: Sure. That'd be
22 great.

23 MR. WOODSMALL: Can I get a copy of
24 it if we're going to ask questions about it?

25 MR. FISCHER: Yeah. Well, we can

1 make it an exhibit later if you like.

2 MR. WOODSMALL: That doesn't help me
3 now.

4 MR. FISCHER: Oh, okay.

5 THE WITNESS: Can I take a quick
6 look at it and give it back to you?

7 MR. FISCHER: Judge, if we can just
8 mark that as an exhibit and I can put it up
9 there for everybody?

10 JUDGE DIPPELL: Sure. We'll mark
11 the exhibit from Mr. Fischer's opening on this
12 issue as Exhibit 57.

13 MR. WOODSMALL: Your Honor, is this
14 a demonstrative exhibit or how are we handling
15 this?

16 MR. FISCHER: It was originally, but
17 I have a witness that can sponsor the data on
18 it.

19 JUDGE DIPPELL: It is demonstrative
20 until it's offered as something different.

21 (SPIRE EXHIBIT NO. 57 WAS MARKED FOR
22 IDENTIFICATION.)

23 THE WITNESS: What this shows, so
24 the orange -- the dark blue line shows the
25 appreciation of the S&P 500 over five years.

1 Total appreciation is 74.9 percent. The top
2 line, the gray line shows the average
3 appreciation for peers identified by Spire.
4 It's 101.07 percent.

5 CHAIRMAN HALL: And those peers,
6 those are what types of companies?

7 THE WITNESS: They are LDCs, local
8 gas distribution companies. And if I'm wrong,
9 someone can correct that later, but I believe
10 they're all LDCs.

11 MR. WOODSMALL: Your Honor, I'm
12 going to object. I believe we have a witness
13 here testifying on facts that are not in
14 evidence and saying if I'm wrong, someone else
15 can correct me. She's clearly testifying on
16 things outside her firsthand knowledge. So if
17 you want to lay a foundation, we can, but I
18 don't believe a foundation has been laid yet for
19 her to testify on the material in Exhibit 57.

20 CHAIRMAN HALL: Well, let me -- what
21 witness do you have that will be able to
22 testify?

23 MR. FISCHER: Steve Rasche is
24 available, and he's the chief financial officer
25 of Spire, Inc., and he can testify to this

1 document and how it was prepared but --

2 CHAIRMAN HALL: Okay. Well,
3 objection sustained.

4 MR. WOODSMALL: Thank you.

5 CHAIRMAN HALL: No. That's fair
6 enough. I should be asking that witness those
7 questions.

8 THE WITNESS: I can talk about the
9 numbers, but --

10 CHAIRMAN HALL: I'm sorry?

11 THE WITNESS: I said I can talk
12 about the numbers.

13 BY CHAIRMAN HALL:

14 Q. Well, then answer -- answer this if you
15 can: Putting aside the validity of these
16 numbers and where they came from, what -- what
17 am I to gather from them of significance when
18 trying to determine what is the proper ROE in
19 this -- or return on equity in this case?

20 A. Okay. Two points. The first is that
21 Spire, which is the orange line, the SR line,
22 that their market price appreciation over the
23 last five years has first -- was under, below
24 the market and below the peer group until about
25 2015 when it rose, and it's now tracking very

1 well with the S&P 500. But it is still below
2 and it is well below since 2015 the peer group
3 against which it's measured, which is considered
4 comparable in risk.

5 Q. So why shouldn't I look at this --

6 A. Second point.

7 Q. Why shouldn't I look at this and say
8 wow, it looks like the ROE -- it looks like
9 Spire's doing comparable -- comparably with the
10 S&P 500 and perhaps there's something going on
11 with -- in other states, other state commissions
12 that is awarding an ROE that is too high and
13 that's why the peer average is so much higher
14 than the S&P 500? Why shouldn't that be my
15 conclusion?

16 A. No, because ROEs, the award isn't -- in
17 my opinion is not as important as the
18 performance, whether the companies are able to
19 earn those ROEs, plus there are many factors
20 that go into the investor assessment of what
21 market price they're willing to pay.

22 This would tell the investor that Spire
23 hasn't first -- for whatever reason, has not
24 been performing as well in the market and is not
25 necessarily as attractive an investment, because

1 they can get a better return by moving to the
2 peer group.

3 But then, as I have done in my
4 testimony, no proxy group is identical in risk.
5 One needs to do an assessment of the relative
6 risk.

7 Q. Tell me what's wrong with the approach
8 that Staff is advocating, that Staff went back
9 and looked at an ROE determination in two recent
10 cases of an approximately 9.5 and then did an
11 analysis of the risk inherent for investors with
12 Spire versus those two electric utilities and
13 Staff determined that the risk was lower and so
14 therefore, reduced the recommendation. But just
15 not the analysis itself, not the numbers itself,
16 but what's wrong with that approach?

17 A. In my opinion, it's an ad hoc approach.
18 For one, you're going back to a return that was
19 authorized under different economic conditions
20 with a different evidentiary record, and I
21 believe one of them was a settled case and one
22 was litigated.

23 What Staff did, in addition to saying
24 that, you know, integrated electrics are less
25 risky than just gas distribution companies, made

1 an ad hoc -- 25 basis points without an analysis
2 just by looking at what ROEs had been in the
3 past and then also added to its analysis that
4 interest rates have fallen since the --
5 especially since the KCP&L case in May, and
6 based on that, well, if you award -- this is my
7 words, my interpretation of what Staff did.
8 Well, if you're going to award 9.5 in May,
9 interest rates have come down, gas is less
10 risky, it should be a lower return without --
11 but that is not what Staff's analysis showed
12 when Staff did its analysis of the market data,
13 and it's not what I show based on my analysis of
14 the market data, and it's not what Mr. Gorman
15 shows based on the analysis of market data.

16 In fact, my analysis, the 10 percent
17 for the proxy group that I had before the
18 adjustments has now risen to 10.35. Beta risk
19 has risen, the equity risk premium has risen.
20 You can't just take one or two factors that go
21 into the ROE, the estimation of the ROE and then
22 say, oh, at this point in time, it was this, the
23 Commission determined this, or somebody
24 estimated it as this, and oh, interest rates
25 have changed and they're less risky, and

1 therefore, it should be X basis points lower.

2 **Q. Tell me why LDCs are less risky than**
3 **vertically integrated electric utilities?**

4 A. Well, as I said earlier, it's the
5 generation portion. That generation is
6 considered less risky production, you know,
7 sales issues, contract issues and water is
8 similar because there's production issue --
9 production factor there as well.

10 Gas, you purchase gas, you don't have
11 any fuel cost issue there, because it's
12 generally a pass-through and is really just the
13 distribution becomes an infrastructure issue.
14 If you have the aging of the pipes and things
15 like that, you have consumption, you have
16 declining consumption issues, but it's a pretty
17 straightforward operation as compared to
18 generation.

19 **Q. So the existence of a PGA reduces risk**
20 **for the LDC?**

21 A. In and of itself?

22 **Q. Yes.**

23 A. In and of itself, again, all else
24 equal, yes.

25 **Q. That's inherent in the question.**

1 A. But my point is that you can't quantify
2 by what basis points that would do that. It
3 would be -- the reduction of risk is reflected
4 in the market data.

5 **Q. Does the existence of an ISRS reduce**
6 **risk?**

7 A. Yes. And that's reflected in the
8 market data as well.

9 **Q. Does the existence of additional**
10 **trackers reduce risk?**

11 A. Yes. And that's reflected in the
12 market data because you find that generally, the
13 estimated borrowing based on the models for gas
14 distribution companies is generally lower than
15 the integrated electricians.

16 **Q. If we were to institute some type of**
17 **RSM in this case, would that reduce risk?**

18 A. Yes. But again, that's imbedded in the
19 market data and especially the proxy group that
20 I use, where the majority have such mechanisms.

21 **Q. If we were to increase the customer**
22 **charge, would that reduce risk?**

23 A. Yes. But again, it can't be quantified
24 in terms of basis points on ROEs. It would be
25 reflected in the market data.

1 **Q. Are there other issues in this case**
2 **before us that -- you know, if we were to**
3 **rule one way or the other would reduce risk?**

4 A. Not of which I'm aware, and the
5 reduction in risk always has to be relative to
6 the proxy group that is being used to estimate
7 the ROE.

8 **Q. Do you think risk is the most**
9 **significant thing that the Commission should be**
10 **focused on when setting an ROE?**

11 A. Oh. If I may answer it this way: I
12 think it is the most important thing to focus on
13 when analyzing the data, the ROE analysis, but I
14 recognize that there are many other factors that
15 go into Commission decision-making; factors
16 about avoiding rate shock, fairness and things
17 like that, and if you have other considerations
18 to take into account, there are other factors in
19 the rate case that I am not an expert in and I'm
20 not testifying to that is more in your purview
21 of judgment than in mine, but when estimating
22 the ROE and the analysis that's been presented
23 to you on ROE, I think you -- it's very
24 important that you look at whether there's been
25 a proper risk assessment.

1 Q. On page 17 of Staff's cost of service
2 report, Mr. Murray -- I believe it was
3 Mr. Murray --

4 A. Yes. I'm there.

5 Q. -- instructs or recommends to the
6 Commission that if -- that the capital structure
7 adopted by the Commission should impact the ROE
8 determination as well on lines 8 through 13 on
9 page 17. Do you see that?

10 A. Yes. Yes, I do.

11 Q. Do you agree with that analysis?

12 A. I agree with the concept without
13 speaking to the -- this specifically whether it
14 should be up or down that the capital structure
15 is certainly a component of the risk I was
16 discussing before, because the greater the
17 amount of debt in the capital structure, the
18 greater the financial risk. Therefore, the
19 greater in general the cost of debt and the
20 greater the cost of equity.

21 So that is a factor that is considered
22 by investors. So that is a risk that you should
23 consider as well. I did not make an adjustment
24 for financial risk because the proposed capital
25 structure was similar to the capital structure

1 of my proxy group.

2 Q. Okay. And you may have alluded to this
3 a moment ago, but I want to be sure I
4 understand. On that same page, lines 3
5 through 8 on page 17, Mr. Murray discusses the
6 credit rating.

7 A. Um-hum.

8 Q. The credit rating is higher for the gas
9 companies vis-à-vis the electric companies?

10 A. Correct, minimally. It's one to -- one
11 and a half notches higher.

12 Q. And is that something that the
13 Commission should take into account in this case
14 when -- when setting a ROE?

15 A. I think it's one component because it's
16 one component that the witness has taken into
17 account and I -- again, I did not make any
18 adjustment because the bond rating of Spire
19 Missouri is the same as the -- my proxy group.

20 Q. But if the Commission were to determine
21 that the consolidated capital structure is
22 appropriate, what type of adjustment would you
23 make in your ROE recommendation, if any?

24 A. All right. I'll look back and tell
25 you. Generally, when I make an adjustment for

1 credit risk, I look at the different notches. I
2 look at the spread between being A2 and a BAA2.
3 There are three notches. So if there were -- if
4 you're looking at a company with a BAA2 versus a
5 company with an A2, it would be the full -- the
6 full spread.

7 This is based on his A to A- and the
8 B -- BBB+. That's about one-sixth of the
9 spread. It's halfway between the notches. And
10 based on my analysis at the time, spreads of BAA
11 -- Moody's BAA over A was 52 basis points. So
12 one-sixth of that, it would be one -- it would
13 be about seven or eight basis points if I were
14 to make a credit risk adjustment solely on those
15 bond rating differences.

16 **Q. Do you know when the Liberty rate case**
17 **determination took place where there was a 10.0**
18 **ROE awarded referred to by counsel?**

19 A. I believe it was at the end of 2014.
20 Subject to check.

21 **Q. What do you believe has happened to the**
22 **capital market since the end of 2014 that**
23 **would -- that would motivate us, the Commission,**
24 **to award a higher ROE?**

25 A. Well, first and foremost, the Federal

1 Reserve has begun to raise interest rates and is
2 now reducing liquidity in the capital markets by
3 reducing its balance sheet. It is expected --
4 if the government doesn't shut down this week --
5 that they will raise another 25 basis -- 25 to
6 50 basis points this week with both value line
7 and blue chip expecting two to three more in
8 2018, even given the fact that Janet Yellen will
9 no longer be Chairman once the new fellow is
10 confirmed. He is of the same perspective that
11 she is, and he is expected to maintain the same
12 policy. That's one thing.

13 The other is we are living in a geo- --
14 be global geopolitical risk has increased for
15 all markets. We are -- in fact, this morning I
16 think I read or I did read that the Nobel Peace
17 Prize winners who were all council -- I don't
18 remember the name -- to stop the proliferation
19 of nuclear weapons is calling for -- you know,
20 is fearful that we -- we may have a nuclear war.

21 We -- I think those factors are bearing
22 very greatly on the market, and we haven't seen
23 what is happening. There is a lot of discussion
24 in the market that the appreciations like this
25 (indicating to Exhibit 57), that the market is

1 gradually reaching a high bubble and may burst.

2 And notwithstanding the low level of
3 interest rates, there is still -- and the low
4 volatility because the market keeps moving
5 steadily up, there's a great deal of risk out
6 there, and personally, I think people are
7 seeking to get returns now because they don't
8 think they're going to last. But I think that
9 in the --

10 **Q. Those are the two factors?**

11 A. Those are two, yeah, that -- um-hum, I
12 think.

13 **Q. Okay. And then this may be the end of**
14 **my inquiry. On page 15 of the cost of service**
15 **report, lines 6 through 13 --**

16 A. Yes.

17 **Q. -- and I'm not going to read that into**
18 **the record. It's -- I'm wondering if you could**
19 **read that and tell me if you --**

20 A. What lines again, please?

21 **Q. 6 through 13.**

22 A. Okay.

23 **Q. If you agree with that analysis?**

24 A. You want me to stop at the end of the
25 sentence, "environment"?

1 **Q. Why don't you read the whole paragraph.**

2 A. Okay. "Goldman Sachs" --

3 **Q. Just to yourself.**

4 A. Oh, I'm sorry. Okay. Never mind.

5 (Reviewing document.)

6 Okay.

7 **Q. What is your reaction to that?**

8 A. Um... (reviewing document.)

9 I have -- oh, never mind -- strike
10 that.

11 I think I respond in my rebuttal that
12 utility COE, cost of equity, is low precisely
13 because interest rates are low because of the
14 way the interest rates affect the estimation of
15 the cost of equity. I'm not convinced that the
16 cost -- investors' required return is low. The
17 estimation of that return using the DCF and the
18 CAPM is low. Interest rates come into play
19 directly in both risk premium methods and the
20 capital asset pricing method and market
21 valuations, based -- the high market valuations
22 based on the low interest rate environment come
23 into play in the low dividend yields we have
24 now.

25 That being said, this is -- I was

1 responding to you earlier, the Federal Reserve
2 is expected to increase the interest rates, and
3 I think treasury bonds are expected to be in the
4 4 percent range within five years. So I think
5 you will begin to see that the cost of equity
6 models will begin to show an increase in the
7 estimated cost of equity.

8 Blue chip is projecting that by the
9 fourth quarter of 2018, the 30-year treasury
10 will be at 4 -- 3.5. By 2020, it will be 4.1,
11 going out to about 4.2 by 2023. And similarly,
12 value line is projecting the same.

13 Oh, and my other point was that if you
14 go back to this chart, and I don't have the
15 exhibit number marked on it, but I don't believe
16 that -- never mind. I'm going to strike that
17 without knowing for sure. Never mind.

18 CHAIRMAN HALL: Okay. I have no
19 further questions, thank you.

20 COMMISSIONER KENNEY: No questions for
21 me.

22 JUDGE DIPPELL: Commissioner Rupp.

23 QUESTIONS BY COMMISSIONER RUPP:

24 Q. Good morning.

25 A. Good morning.

1 **Q. Can you remind me what the beta on a**
2 **stock is?**

3 A. The beta is an estimate measurement of
4 something called systematic risk,
5 non-diversifiable risk. It's the measure of --
6 to get wonky here -- the co-variability of a
7 stock's returns or equity risk premiums relative
8 to the market as a whole. It's not a complete
9 measure of risk. It -- the R-square associated
10 with it is only about 20 percent. The rest of
11 the risk that is reflected in the volatility of
12 returns is -- would be non -- nonsystematic or
13 company-specific non-diversifiable risk.

14 **Q. Okay. Your beta is relative to the S&P**
15 **500 risk. So if I have 1.0 beta, I'm right**
16 **there with the S&P 500 on a risk standpoint?**

17 A. Correct. And you have to remember that
18 that 1.0 -- it's always 1.0. From year to year
19 the market is 1.0, where its risk might change.
20 If you look at a 1.0 beta, you say, "Oh, the
21 risk never changes," but it does. It's always
22 assumed to be 1.0.

23 **Q. And then the beta for Spire is .53**
24 **currently?**

25 A. Um... I don't believe so. Value line

1 has it at .70. You may be looking at an
2 unadjusted beta.

3 Q. I was looking just at a market watch or
4 something.

5 A. I think those are unadjusted.

6 Q. Unadjusted?

7 A. Right.

8 Q. Okay. So unadjusted, it's point -- or
9 adjusted, it's .7 or something?

10 A. As of the September 1st value line, it
11 was .70.

12 Q. .70. So according to the value line
13 then, that would be less risky compared to the
14 market as a whole?

15 A. Correct. If the market moves, say goes
16 up 10 percent, it's going to go up 70 or vice
17 versa.

18 Q. Okay. And I could not see the chart
19 that was shown this morning --

20 A. Oh.

21 Q. -- because I was listening on the drive
22 in, but what is the return of the S&P 500 in
23 that chart?

24 A. There's not a return. It's just a
25 total increase over the five years. But what

1 beta measures, based on this chart, is the
2 variability, the up and down for each of the
3 lines. Relative to the up and down, the change
4 in the blue line, the S&P 500.

5 Q. But over that period of time, the S&P,
6 it rose 74.9 percent according to this chart?

7 A. Correct.

8 Q. And Spire's stock was up 73.6? So
9 it --

10 A. Correct.

11 Q. With less risk, it still tracked the
12 market as a whole?

13 A. But -- yes, based on the pure CAPM
14 theory, but the peer group, who is my peer
15 group, all of which are in this group, their
16 beta is -- their average beta is about .71 right
17 now. But as I said in response to one of your
18 earlier questions, beta risk is only 20
19 percent -- explains only 20 percent of that
20 volatility.

21 Q. So let's walk down that road. So if
22 the average of the peer group is .71, so roughly
23 in line with Spire, that the entire peer
24 group -- how did the entire peer group do
25 compared to the S&P 500?

1 A. This peer group did 101 percent or
2 difference of 26, 27 basis points better.

3 **Q. Okay. So with the same risk premium or**
4 **the same level of risk, the peer group did**
5 **better than the market?**

6 A. That's only assuming that you're
7 looking at beta risk, but that's only one factor
8 of risk.

9 **Q. We're just looking at beta risk right**
10 **now?**

11 A. Just -- yes. The math is correct on
12 that.

13 **Q. Okay. Great. So explain to me why if**
14 **the beta risk in the peer group's beta risk and**
15 **is tracking the market, they're getting a return**
16 **above the market and stuff, why a need for a**
17 **risk premium is there, in your opinion, for an**
18 **investor?**

19 A. It is not there based on beta risk. It
20 is there based on those other -- the other
21 component.

22 **Q. Then explain to me what those other**
23 **risks are besides the beta risk?**

24 A. Well, okay. The only adjustment I made
25 for that type of risk was for size, because all

1 else equal and when one picks a proxy group, one
2 assumes that that company is as similar as
3 possible in risk to the target company, the
4 regulated company, to Spire, but no company can
5 be -- no proxy group can be. But based on the
6 size, Spire is smaller and there are -- there is
7 empirical quantitative evidence out there that
8 indicates that you can determine approximately
9 how large that premium -- or small that
10 premium -- or whether there should be a premium
11 at all.

12 And I think I've been in this
13 Commission for Missouri American and actually
14 didn't put one in or put a negative one in
15 because their size was bigger than me, the proxy
16 group at the time.

17 Those are the other risks. That is not
18 the only risk, different business risk that may
19 be seen by investors. As I said, they look at
20 many more. One is regulatory environment.
21 That's a big -- and cost recovery, big factor in
22 credit ratings. Like 50 percent of the credit
23 rating processes evaluates regulatory
24 environment and cost recovery.

25 **Q. And so without me having to dig into**

1 your testimony again, what is the quantitative
2 size difference of Spire to the peer group?

3 A. I believe it's 34 basis points, I
4 believe. I can look it up.

5 Q. And so you just took the 34 basis
6 points of --

7 A. (Shaking head.)

8 Q. So that's where you came up with your
9 adjustment?

10 A. I used that, but it's a very kind of --
11 the comparison of the premiums, the size
12 premiums for the group and for Spire fit kind of
13 very grossly into deciles. They're broad. So
14 I... it was 32 basis points and my adjustment
15 was 20. I took something less than half of
16 that.

17 Q. Okay. Switching gears to the goodwill,
18 are you the person I should ask on that or is
19 that --

20 A. No. That's Mr. Hevert.

21 Q. Okay. Mr. Hevert. I'll save my
22 questions for that.

23 A. Thank you.

24 JUDGE DIPPELL: Is there further
25 Cross-Examination based on questions from the

1 Bench from Staff?

2 MR. MILLS: Judge, before we get to
3 that -- I didn't want to interrupt the
4 Commissioner's questions -- what I want to make
5 clear on the record that what we are calling for
6 purposes of questions "the peer group" has no
7 foundation. We don't at this point know what is
8 in that group or how the returns for that group
9 were calculated.

10 So I think the record needs to clearly
11 reflect that in those series of questions,
12 that's what we're talking about. We're talking
13 about some unknown group determined by someone
14 other than this witness and whose returns are
15 were calculated by someone other than this
16 witness.

17 JUDGE DIPPELL: And that's with
18 regard to the peer group that is shown on
19 Exhibit 57?

20 MR. MILLS: Exactly.

21 JUDGE DIPPELL: I'll just clarify
22 with the witness, however, when you talk about
23 your peer group --

24 THE WITNESS: I try to use the word
25 "proxy group."

1 JUDGE DIPPELL: You used the word
2 "proxy group," and you were discussing the proxy
3 group from your testimony.

4 THE WITNESS: Correct.

5 COMMISSIONER RUPP: And that's what
6 I was referring to your proxy group in your
7 testimony.

8 THE WITNESS: Okay.

9 JUDGE DIPPELL: Right.

10 All right. Is there further
11 Cross-Examination from Staff?

12 MR. THOMPSON: Just a little bit.

13 Thank you, Judge.

14 RE-CROSS-EXAMINATION BY MR. THOMPSON:

15 Q. Referring to Exhibit 57, in response to
16 a question from the Chairman, you testified that
17 the exhibit shows that Spire wasn't doing as
18 well as the peer group; isn't that correct? Do
19 you remember that?

20 A. Yes.

21 Q. Okay. But it's true, isn't it, that
22 investors may use Spire as more risky because of
23 its acquisition activity?

24 A. I don't agree with that. They may.

25 Who knows. Who knows. It's in the market data.

1 However --

2 MR. THOMPSON: Thank you very much.

3 You've answered my question.

4 JUDGE DIPPELL: Is there further
5 Cross-Examination by Public Counsel based on the
6 questions from the Bench?

7 MR. SMITH: Yes. I just had a
8 question about the geopolitical risk.

9 RE-CROSS-EXAMINATION BY MR. SMITH:

10 **Q. I wanted to clarify. Did you say**
11 **earlier that Spire should have a higher ROE**
12 **because of the risk of nuclear war?**

13 A. No. No. I said that the markets in
14 general are riskier and that would affect all
15 companies.

16 MR. SMITH: Okay. Thank you.

17 JUDGE DIPPELL: MIEC.

18 MR. WOODSMALL: Yes. Thank you,
19 your Honor.

20 RE-CROSS-EXAMINATION BY MR. WOODSMALL:

21 **Q. Can you tell me how interest rates have**
22 **changed since 2014?**

23 A. They have been going up and down in a
24 very general --

25 **Q. But since 2014.**

1 A. -- very narrow range.

2 Um... (reviewing document.)

3 **Q. You don't know?**

4 A. Off the top of my head, no.

5 **Q. So when the Chairman asked you what has**
6 **changed since the Commission issued its decision**
7 **in 2014 and you said interest rates have gone**
8 **up, you don't know that interest rates have gone**
9 **up since 2014?**

10 A. I was referring to the increases in
11 the -- that Federal Reserves has made, and that
12 has affected interest rates. So in general.
13 They are going up and the forecasts are going
14 up, but specifically, no.

15 **Q. You don't know if interest rates --**

16 A. Right.

17 **Q. -- have gone up since 2014?**

18 A. I didn't go back and see what they were
19 in 2014 compared to now.

20 **Q. If interest rates had gone down**
21 **relative to when the Commission issued its**
22 **decision in Liberty utilities in 2014, one would**
23 **expect ROE to be less; is that true?**

24 A. Not necessarily. The estimation may be
25 lower, because as I said before, that the

1 estimation of the models is based in part on
2 interest rates because they form part of the
3 components and they form part of the reason
4 market valuations are rising, but there are
5 other factors that go into the ROE, investors'
6 perception of risk being one of them.

7 **Q. But all else being equal, interest**
8 **rates go down, ROEs go down?**

9 A. I can't answer that. All else equal is
10 never equal.

11 **Q. Okay. So when you were asked all the**
12 **questions from the Chairman about all else equal**
13 **and you kept placing the caveat "all else**
14 **equal" --**

15 A. Yeah.

16 **Q. -- you don't know that --**

17 A. Well, if all else equal, what happens
18 when interest rates go down? If interest rates
19 go down about a hundred percent, a hundred basis
20 points, theoretically, the cost of equity, the
21 equity risk premium rises by 50 basis points.
22 They move in tandem, but they move at an in-risk
23 relationship.

24 So it doesn't go down as far. If
25 you're just going to do the math that way, you

1 got a cost of equity, say 10 percent, you have a
2 debt cost of 5 percent, it goes down to
3 4 percent, 10 percent goes to 9.5. It doesn't
4 go down to 9.

5 **Q. They move proportionately to each**
6 **other?**

7 A. In an inverse way, yes. Oh, I'm --
8 yeah, that's right.

9 **Q. Can you tell me what Spire's credit**
10 **rating is?**

11 A. I believe it's in A. (Reviewing
12 document.)

13 I have it as an A1/A2 by Moody's, and
14 an A- by S&P.

15 **Q. Do you know what Ameren's credit rating**
16 **is?**

17 A. Not off the top of my head.

18 **Q. Do you know what Great Plains' credit**
19 **rating is?**

20 A. No. Not -- not -- I don't have it with
21 me now.

22 **Q. Okay. Would you agree that credit**
23 **rating is a reflection of risk?**

24 A. It's a reflection of default risk and
25 the risk that the bondholders face. It is -- in

1 general, it can give an indication of the risk,
2 but it doesn't measure in any way equity risk.

3 **Q. It -- would you agree that you prepared**
4 **your proxy group in large part based upon**
5 **similar credit rating between the companies?**

6 A. Credit rating was not one of my
7 selection criteria.

8 **Q. But you said earlier that Spire's**
9 **credit rating matched that of your proxy group;**
10 **is that correct?**

11 A. It is correct. I did not select them.
12 The proxy company is based on credit rating.

13 **Q. But the fact that they have a similar**
14 **credit rating reflects that they are comparable**
15 **companies; is that true?**

16 A. Correct. In everything but size.

17 **Q. Okay. And would you agree that as a**
18 **company's credit rating goes up, its ROE tends**
19 **to go down?**

20 A. Yes. In general --

21 **Q. And --**

22 A. -- it may. It may. Again, I'll put
23 all else equal on it. It may; it may not,
24 depending on investors' perception of the risk.

25 **Q. So if Spire has a higher credit rating**

1 **than Ameren and Great Plains, all else being**
2 **equal, it would require a lower ROE?**

3 A. Again, we're back to talking about
4 probably an authorized ROE. You -- we really
5 want to emphasize -- you need to look -- one
6 needs to look at the evidence in the record
7 relative to what the market data of companies of
8 similar risk, what we see their required returns
9 by investors are.

10 **Q. But if Spire has a higher credit rating**
11 **than Ameren and Great Plains, it has a lower**
12 **risk?**

13 A. It has a lower credit risk.

14 **Q. Right. And as credit risk goes down,**
15 **the expected authorized return goes down, I**
16 **believe you said earlier?**

17 A. I didn't say "expected authorized
18 return."

19 **Q. Okay. Would -- do your recommended**
20 **returns go down as credit rating goes down?**

21 A. My recommended return is based solely
22 on the market they'd apply to the proxy
23 companies. I believe I was asked a question
24 earlier about -- or we discussed if there
25 were -- what kind of credit. I think it was

1 relative to Mr. Mahr's (phonetic) Staff report,
2 the double -- the BBB+ and the A/A-, what kind
3 of adjustment would be made. If there were to
4 be a significant difference in the bond ratings
5 of the companies and I didn't have size or -- or
6 not size, I'm sorry -- capital structure
7 differences, there may need to be a credit risk
8 adjustment up or down, but the basic ROE is
9 based on the application of the models to the
10 market data. For example --

11 **Q. But you --**

12 A. Yeah.

13 **Q. -- determined the market data based**
14 **upon a proxy group that has the same credit**
15 **rating as Spire in this case?**

16 A. Yes.

17 **Q. Okay.**

18 A. And that was -- but I didn't select
19 them that way.

20 **Q. Okay. An -- and -- I can do redirect.**
21 **And you don't know how Spire's credit**
22 **rating compares to Ameren's and Great Plains?**

23 A. Ameren and Great Plains are irrelevant
24 to my analysis.

25 **Q. But it's relevant to how investors**

1 invest; is that true? Investors don't only have
2 the option to invest in your proxy companies.

3 A. Correct. But they're not going to
4 consider only credit ratings as the only
5 difference.

6 Q. And you were undertaking some analysis
7 on the fly -- excuse that characterization --

8 A. It's okay.

9 Q. -- about how ROEs would change based
10 upon changes in capital structure. Do you
11 recall that? I believe you were saying --

12 A. Yes.

13 Q. -- something about one-sixth of the
14 differential?

15 A. That was credit rating difference, yes.

16 Q. Okay. And -- okay. So your attempt to
17 assess a change in ROE was based upon credit
18 rating differences?

19 A. Yes. That six or seven rate basis
20 points was based on credit rating. I was
21 specifically asked what an adjustment would be
22 for the A/A- to BBB+, if I could identify that.

23 Q. And A to A- to BBB+, what did you say
24 was the difference in ROE?

25 A. It would be one-sixth of 52 basis

1 points, but it's only relative --

2 **Q. So approximately nine basis points?**

3 A. Maybe nine, yes.

4 MR. WOODSMALL: Okay. I have no
5 further questions.

6 THE WITNESS: But that's only
7 relative to this analysis.

8 MR. WOODSMALL: Thank you.

9 JUDGE DIPPELL: Is there anything
10 from MIEC?

11 RECROSS-EXAMINATION BY MR. MILLS:

12 **Q. Is in fact the credit rating for your**
13 **proxy group and Spire exactly the same?**

14 A. I believe so, yes.

15 **Q. By both S&P and Moody's?**

16 A. No. The average for the proxy group is
17 A2, but it is A- for the -- for S&P.

18 **Q. Okay. But Moody's considers Spire to**
19 **be more creditworthy than the proxy group,**
20 **correct?**

21 A. Minimally.

22 **Q. But in that direction, correct?**

23 A. If you're going to look at spreads,
24 yes, there would be just a little -- a one -- a
25 little, bitty bit, yes.

1 **Q. You didn't make any adjustment for**
2 **that, though, did you?**

3 A. No, I did not.

4 MR. MILLS: No further questions.

5 JUDGE DIPPELL: Is there anything
6 from the Environmental Defense Fund?

7 MS. KARAS: No, Judge.

8 JUDGE DIPPELL: Is there Redirect by
9 Spire?

10 MR. FISCHER: Just a little, Judge.

11 REDIRECT EXAMINATION BY MR. FISCHER:

12 **Q. Ms. Ahern, let's start with some of the**
13 **later questions and go backwards, if that's all**
14 **right.**

15 A. That's fine.

16 **Q. I believe it was Commissioner Rupp**
17 **asked you some questions regarding the betas and**
18 **also asked you a question about the fact that**
19 **the peer group had performed better than Spire's**
20 **performance over the last five years. Do you**
21 **recall that question?**

22 A. Yes.

23 **Q. What is the better performance of the**
24 **peer group tell you about relative to Spire?**

25 MR. MILLS: Judge, I'm going to

1 object to the characterization of this peer
2 group. We don't know in what sense it's a peer
3 group, and he wants to qualify it by saying this
4 unknown group that's labeled "Peer group,"
5 that's one thing, but I think coming from the
6 Company attorney calling it a peer group assumes
7 facts not in evidence.

8 MR. FISCHER: Judge, again, we're
9 going to have a witness to sponsor that and just
10 as a matter of expediency here to get through
11 the cross, I would like to be able to reference
12 the peer group as it's reflected on that
13 exhibit.

14 MR. WOODSMALL: I believe he just
15 proved the point. He said -- Mr. Lewis's [sic]
16 objection was assumes facts not in evidence, and
17 he just conceded that the facts will come in
18 later, so...

19 MR. FISCHER: And, Judge, that
20 happens all the time in this hearing room, where
21 we put one witness up and then 15 witnesses
22 later, we put somebody else's testimony in. He
23 can move to strike it if we can't support it.

24 JUDGE DIPPELL: I'm going to allow
25 the question. You might want to, just for the

1 record, keep it clear that you're discussing
2 the --

3 MR. FISCHER: Exhibit.

4 JUDGE DIPPELL: -- reference to the
5 peer group on that exhibit.

6 BY MR. FISCHER:

7 Q. Ms. Ahern, you understand that caveat?

8 A. Yes.

9 Q. What does the better performance of
10 that specific peer group on Exhibit 57 tell you
11 relative to Spire's performance?

12 A. It tells me that Spire's performance,
13 Spire has been underperforming the peer group,
14 which is -- I do understand it's a group of
15 LDCs.

16 Q. Does -- you mentioned in answer to -- I
17 think it was the Chairman that you made an
18 adjustment due to size of Spire. Would you
19 explain why you did that?

20 A. Because size is a factor of a risk
21 factor, what in regulation -- and this kind of
22 goes a little bit to the capital structure issue
23 as well and to some of the opening comments.

24 Rates are being set in this proceeding
25 for Spire, for Spire Missouri only. They're not

1 being set for Spire Energy. It is the use of
2 funds which is important to -- that gives rise
3 to the risk of that investment. The risk here
4 is related only to Spire's operations, to
5 Spire's rate base. We pick a proxy group. It's
6 not related to Spire, Inc., and while Spire,
7 Inc. has the shared services agreement, and as I
8 said in either rebuttal or surrebuttal, it
9 mitigates the effect of that risk on the
10 consumers by lowering the costs.

11 If Spire were to be spun off and be an
12 independent, standalone company, those costs
13 would be higher, the risk would be the same, but
14 the costs would be higher and the rates to --
15 rates for ratepayers would be higher.

16 Size is one of the -- I think it is the
17 maybe other than credit risk, and financial
18 risk, it's the -- to the best of my knowledge,
19 the only risk difference that can be quantified
20 and that has been empirically quantified.

21 What I've done is I've used one of
22 those empirical studies to determine size of
23 premium relative to the market associated with
24 the proxy group and a size premium relative to
25 the market for Spire based on their relative

1 sizes. I subtract those two and got 32 percent
2 or 32 basis points, and then I took a portion of
3 that 20 basis points.

4 **Q. Is the regulatory risk environment**
5 **another risk that would be taken into account?**

6 A. Yes, it would, and as I said earlier,
7 it is one of -- it's 25 percent of what it
8 affects, I should say, the credit rating
9 analysis of both S&P and Moody's by about
10 25 percent.

11 **Q. Within that regulatory risk category,**
12 **what kind of things are typically considered by**
13 **analysts?**

14 A. One of the most important is cost
15 recovery -- you know, cost recovery mechanisms
16 which will enable and allow the earning of the
17 authorized return. The authorized return, if
18 it's a surprise, can be -- I've seen cases where
19 an ALJ has recommended a 10.2 and it's been
20 brought down to, say, 9.5 and caught the market
21 and caught the credit analysts by surprise, and
22 that was credit negative.

23 Transparency, consistency, even if that
24 consistency is negative, you know, consistently
25 low ROEs, you know what you're going to be

1 getting, if the ROE is so low that it's going to
2 put the Company in financial distress and begin
3 to put pressure on cash flows and credit
4 metrics, those sorts of things.

5 **Q. And I believe the Chairman asked you**
6 **about things like the existence of a PGA and the**
7 **ISRS and trackers and how that affected the**
8 **risk. Do you recall that?**

9 A. Yes, I do.

10 **Q. Would your proxy group -- what I'm**
11 **talking now about is the companies that you**
12 **actually use to compare Spire to in your**
13 **testimony.**

14 **Would those companies also have those**
15 **types of regulatory mechanisms available to**
16 **them?**

17 A. Yes, they do, and I've -- there's a
18 schedule, I think the only schedule attached to
19 my surrebuttal that shows that, and to the
20 extent that those companies do have those kinds
21 of mechanisms, it's reflected in the market data
22 already. So it's reflected in that base
23 10 percent of mine and now currently 10.35.

24 **Q. And to the extent that the Company**
25 **didn't have an RSM or a rate design that was**

1 **weather mitigating, would that affect the risk**
2 **of the Company?**

3 A. Not a quantifiable way because that has
4 not been empirically proved. However, if one's
5 mindset is that you're going to reduce an
6 authorized ROE, and there are some commissions
7 that do because of the existence of these
8 mechanisms, then relative to the proxy group if
9 the Company in question, the target, the Company
10 being regulated for whom rates are being set at
11 that time, if they do not have those mechanisms,
12 logic and symmetry dictates you need to increase
13 the ROE. I'm sorry.

14 **Q. Would decrease in customer service**
15 **charges have an effect on the risk of the**
16 **Company being able to recover its fixed costs?**

17 A. Depends what they did with fixed costs
18 in that case, how it's balanced out. If
19 customer charges are decreased and fixed costs
20 are increased to balance it, it would hurt the
21 customers.

22 **Q. And those are recovered in commodity**
23 **rates then typically; is that correct?**

24 A. Right.

25 **Q. So if you don't recover as much up**

1 front in the customer charges, you're more at
2 risk --

3 A. Right.

4 Q. -- whether you're going to be able to
5 recover them through the commodity rates; is
6 that true?

7 A. Correct. Correct. If you get any
8 fixed charges that are recovered and customer
9 charges as there's declining consumption, then
10 you're going to run the risk of not recovering
11 your fixed charges.

12 Q. The Chairman also asked you about, I
13 think, what has changed since the Commission
14 granted Liberty a 10.0 percent increase -- or
15 ROE in 2014. Do you recall those?

16 A. Yes, I do.

17 Q. I believe you mentioned there were
18 market changes since that time and one of the
19 ones that you mentioned were the Fed -- the Fed
20 had raised interest rates?

21 A. Yes.

22 Q. Do you happen to know how many times
23 roughly that's happened since either 2014 or
24 2015?

25 A. Well, they raised it from what 0 to 25

1 all the way up to 25 to 100, in 25-basis point
2 increments of three or four, with another one
3 expected Wednesday.

4 **Q. Why are you suggesting that there's**
5 **another one expected Wednesday?**

6 A. Um, well, the -- something called the
7 CME FedWatch tool is projecting a 90 to
8 95 percent expectation, the -- as I said, value
9 line and blue chip are expecting it. I read it
10 this morning in the paper, and I think investors
11 are expecting -- I think it will be a big shock
12 to the coun- -- to the market if they don't
13 raise it.

14 **Q. You also mentioned, I think in that**
15 **same discussion, that the Fed was reducing its**
16 **balance sheet. What did you mean by that?**

17 A. They're reducing the securities that
18 they're holding outright, the quantitative
19 easing that they began at the financial crisis.
20 They pumped a lot of money into the market by
21 buying bonds. Now they're selling them again
22 and they are reducing liquidity by taking money
23 out of the market.

24 **Q. What does that tell you about their**
25 **goal, if you want -- if you use that term for**

1 **where interest rates should be?**

2 A. Their goal is to move them back -- not
3 back. They don't think -- they think they're
4 going to be low for sometime, but they -- and
5 they recognize that they're low. In fact, they
6 said in the November 1st press release, which
7 was echoed in their minutes: "The Committee
8 expects the economic conditions will evolve in a
9 manner that will warrant gradual increases in
10 the federal fund's rate: The federal fund's
11 rate is likely to remain, for sometime, below
12 levels that are expected to prevail in the
13 longer run."

14 So they recognize that they are low
15 now.

16 **Q. And what does that tell you -- or what**
17 **would that suggest to you that long-term**
18 **interest rates will do over --**

19 A. That long-term interest rates will
20 increase. While they may not increase to levels
21 they were prior to the financial crisis, they're
22 certainly going to increase above what they are
23 now, and given that the investors' required
24 return of equi- -- cost and equity and
25 rate-making are all expectational, that's my

1 argument, my support for using forecasted
2 interest rates in cost of equity analysis.

3 **Q. I believe you also mentioned one of the**
4 **other factors that have changed have been**
5 **authorized rates of return. Do you recall that?**

6 A. I recall discussions of authorized
7 rates of return, yes.

8 **Q. What has happened since 2014 or 2015 to**
9 **authorized rates of return or even more recently**
10 **than that, if you have that data?**

11 A. Yes, I do. If you look -- I think it's
12 the last page of my surrebuttal, which is 40,
13 there's a chart there from SNL Energy,
14 Regulatory Research Associates that shows
15 litigated LDC authorized ROEs since January 2015
16 through the end of September 2017. They are --
17 and I put a trend line in there to show they are
18 rising. The average for 2017 alone is 9.89
19 percent.

20 **Q. Well, and that was the number I had**
21 **mentioned in my opening; is that right?**

22 A. That's right. Correct.

23 **Q. Okay. There was also some discussion,**
24 **I believe, with the Chairman about the capital**
25 **structure issue?**

1 A. Yes.

2 Q. Would using an artificially low equity
3 component have an effect on overall risk?

4 A. Yes, for two reasons -- and two
5 reasons. Number one, if a company actually had
6 an overall equity component that was, you know,
7 significantly lower than its peers, it would
8 have significantly greater risk. If Spire is
9 authorized an equity ratio that is significantly
10 lower than its actual ratio and lower than its
11 peers, that will be perceived negatively in my
12 opinion by -- by the market and by credit rating
13 agencies because there would be -- the Company
14 would have more difficulty servicing the debt
15 which it would -- the debt that would have to be
16 serviced is based on the lower the debt ratio
17 and they would have lower funds to do so.

18 Q. Does a lower debt ratio also affect a
19 credit rating?

20 A. It can. It is one of the factors that
21 they look at. More importantly, I think, if
22 there were an authorization of a lower than
23 actual credit rating -- I mean -- I'm sorry --
24 lower than actual common equity ratio, I think
25 that would affect the credit -- I mean the

1 regulatory environmental portion of the risk
2 analysis.

3 **Q. A lower credit rating could increase**
4 **cost of debt; is that true?**

5 A. Absolutely.

6 **Q. If a commission were to substantially**
7 **change from one case to the next, the capital**
8 **structure that has been used in the past to make**
9 **it less equity in that capital structure, how do**
10 **you think that would be perceived?**

11 A. I believe that the credit rating
12 agencies would perceive that negatively, and I
13 believe RRA would perceive that negatively. Any
14 time that there's a departure from, you know,
15 prior -- I would say prior policy and prior
16 decision-making, that is -- can be detrimental
17 to the Company is generally perceived as -- it's
18 uncertainty and uncertainty is risk.

19 **Q. And what is RRA, for the record?**

20 A. Regulatory Research Associates.
21 They're formerly SNL Energy. They're now owned
22 by S&P Global venture.

23 **Q. And what do they do?**

24 A. They -- RRA analyzes, they keep track
25 of databases of mostly electric and gas. Now

1 they're doing some water regulatory decisions,
2 mechanisms. They provide evaluations of the
3 decisions, they provide evaluations of state
4 commissions, they provide on a quarterly basis a
5 chart of a grading of regulatory commissions.

6 **Q. Okay. Just -- I'm almost done here.**
7 **There was a mention, I think, on recross about**
8 **the -- your discussion about the geopolitical**
9 **risk?**

10 A. Yes.

11 **Q. Would you be more specific about what**
12 **you're talking about there?**

13 A. I'm just talking about the instability
14 globally that we have. Some of the things that
15 the U.S. has done, some of this morning, if you
16 don't know, there was an attempted terror attack
17 on Port Authority in New York. It wasn't
18 foiled. He bumbled it. But we face some
19 significant issues with trade, with sanctions of
20 different countries. NATO is -- is not very
21 happy with us. So...

22 **Q. Are you concerned -- would you have**
23 **included --**

24 A. And in the Middle East and North Korea
25 more importantly.

1 Q. Okay. I believe too you might have
2 been cut off when you were trying to answer a
3 question about whether the acquisition activity
4 of the Company has --

5 A. Right.

6 Q. -- has somehow affected its risk?

7 A. Yes.

8 Q. Could you expand on what you were
9 trying to say?

10 A. What I was going to say is I don't
11 think it really will because the acquisition
12 activity and the expansion has been into
13 regulated natural gas distribution companies and
14 in a state that has a very good regulatory
15 evaluation by RRA is considered very credit
16 supportive and it's a good state to operate in.

17 Q. Do you know if Alabama has a pretty
18 high environ- -- regulatory rating by RRA?

19 A. They do. I don't have it off the top
20 of my head. But I have it here.

21 Q. Okay. Well --

22 A. Yes, they do. They're rated quite
23 high.

24 MR. FISCHER: Judge, that's all the
25 questions I have. I appreciate your indulgence.

1 JUDGE DIPPELL: Thank you. And I
2 believe that's all the questions for you,
3 Ms. Ahern. You may step down and be excused.

4 THE WITNESS: Thank you.

5 (Witness excused at 10:57 a.m.)

6 JUDGE DIPPELL: We are going to go
7 ahead and take a short break and come back at
8 11:10. Go off the record.

9 (Recess taken from 10:57 a.m.
10 to 11:10 a.m.)

11 JUDGE DIPPELL: It's 11:10. We can
12 go back on the record. Okay. We've returned
13 from break, and we are ready to begin with
14 Spire's next witness.

15 MR. PENDERGAST: Thank you, your Honor.
16 At this time we would call Robert E. Hevert to
17 the stand.

18 JUDGE DIPPELL: Mr. Hevert, will you
19 please raise your right hand.

20 (Witness sworn.)

21 THE WITNESS: Yes, I do.

22 JUDGE DIPPELL: Thank you.

23 ROBERT E. HEVERT testified as follows:

24 DIRECT EXAMINATION BY MR. PENDERGAST:

25 Q. Good morning, Mr. Hevert.

1 A. Good morning.

2 **Q. Are you the same Robert E. Hevert who**
3 **has previously caused to be filed in this**
4 **proceeding surrebuttal testimony marked as**
5 **Exhibit 36?**

6 A. Yes, I am.

7 **Q. Do you have any changes or corrections**
8 **to make to your testimony?**

9 A. I've got three typographical errors.
10 So I apologize. They're not at all substantive.
11 The first is at page 6, line 3, toward the
12 right-hand margin, there should be a closed
13 quote after the word "debt."

14 The second is on page 14, line 8, there
15 should be a period after the word "equity." And
16 lastly, page 15, line 19 toward the right-hand
17 margin, the word "ratio" should be plural,
18 "ratios," and those are all my corrections.

19 **Q. Thank you.**

20 **With those corrections, if I were to**
21 **ask you the same questions today that appear in**
22 **your surrebuttal testimony, would your answers**
23 **be the same?**

24 A. Yes, they would.

25 **Q. And are those answers true and correct**

1 to the best of your knowledge and belief?

2 A. Yes, they are.

3 MR. PENDERGAST: With that, your
4 Honor, I would tender Mr Hevert for
5 Cross-Examination and request that his
6 surrebuttal testimony be admitted into the
7 record.

8 JUDGE DIPPELL: And does
9 Mr. Hevert -- is this his only issue?

10 MR. PENDERGAST: It is.

11 JUDGE DIPPELL: All right. Is there
12 any objection to Exhibit No. 36?

13 MR. SMITH: No objection.

14 JUDGE DIPPELL: All right. Seeing
15 no objection, I will admit Exhibit No. 36 into
16 the record.

17 (SPIRE EXHIBIT NO. 36 RECEIVED INTO
18 EVIDENCE.)

19 JUDGE DIPPELL: Is there
20 Cross-Examination by Staff?

21 MR. THOMPSON: Thank you, Judge.

22 CROSS-EXAMINATION BY MR. THOMPSON:

23 Q. Nice to see you, Mr. Hevert.

24 A. Good morning.

25 Q. I wonder if you could tell me what your

1 **hourly rate is?**

2 A. I believe my hourly rate is the same as
3 Miss Ahern's, which would be \$350.

4 **Q. And do you have any idea how many hours**
5 **you've devoted to this case up until now?**

6 A. I don't, but it is of course a limited
7 issue. It came in late in the case. It's not
8 many.

9 **Q. Do you have any idea how many hours**
10 **ScottMadden as a whole has devoted to this case**
11 **so far?**

12 A. I do not.

13 **Q. Or what they've billed so far?**

14 A. Same answer, I do not.

15 **Q. Okay. Now, were you present while**
16 **Ms. Ahern testified?**

17 A. Yes, I was.

18 **Q. And did you hear her testify that there**
19 **was no cap on the charges for ScottMadden with**
20 **respect to this case?**

21 A. I thought her answer was with respect
22 to her testimony, but I may be incorrect on
23 that.

24 **Q. Okay. Do you happen to know whether**
25 **there's any cap or ceiling on how much**

1 **ScottMadden can bill for this case?**

2 A. I don't know whether there's a cap.
3 Quite often we will propose a budget, and I
4 think for the reasons Ms. Ahern noted, quite
5 often the scope of discovery, the scope of
6 rebuttal is unknown at the beginning of a case,
7 so it's difficult to put a firm cap on it.

8 Quite often we'll establish a budget
9 and to the extent we approach the budget, we
10 would then go to the client and talk about
11 whether or not the budget can be increased.

12 As to Ms. Ahern's testimony and some of
13 the other portions of the Company's testimony in
14 this case, I could not say what that budget or
15 limit might be.

16 MR. THOMPSON: Thank you. I have no
17 further questions.

18 JUDGE DIPPELL: Is there
19 Cross-Examination by Public Counsel?

20 MR. SMITH: Yes, Judge. Thank you.

21 CROSS-EXAMINATION BY MR. SMITH:

22 **Q. Good morning, Mr. Hevert.**

23 A. Good morning.

24 **Q. Have you ever testified to a public**
25 **advocate's office?**

1 A. A public advocate?

2 **Q. Yes, such as OPC?**

3 A. I have not, but I'll also say I've
4 never been asked.

5 **Q. So is it fair to say you predominantly**
6 **have testified for utility companies?**

7 A. I would say that my principal testimony
8 has been on behalf of utility companies. I have
9 testified for and been retained by utility
10 commissions in the past, but yes, that's -- I
11 think that's fair to say. But again, my
12 response earlier was not in jest. The point is
13 I have not been asked to provide testimony on
14 behalf of a consumer advocate or an Attorney
15 General or Staff.

16 **Q. You have been -- do you have a copy of**
17 **your testimony in front of you?**

18 A. Yes, I do.

19 **Q. And I understand you only produced**
20 **surrebuttal testimony in this case; is that**
21 **correct?**

22 A. Yes, that's correct.

23 **Q. Would you please go to page 6 of that**
24 **testimony?**

25 A. (Witness complying.)

1 Yes, I'm there.

2 **Q. And my understanding this is not a**
3 **C designation, but you state that the**
4 **acquisition price for MGE was \$1,013 million.**
5 **Isn't that true?**

6 A. What I think -- you're referring to
7 Table 2?

8 **Q. Yes.**

9 A. Right. So Table 2 at this point was
10 the -- the amount shown from the Laclede Group
11 investor presentation as of September 13th --
12 excuse me -- September 2013. As to whether or
13 not that was the actual final purchase price,
14 I'm not entirely sure.

15 **Q. Would you have any reason to doubt that**
16 **the purchase price was approximately that amount**
17 **which appears on your table?**

18 A. That it was approximately that amount?

19 **Q. Yes.**

20 A. And I'm sorry, your question was would
21 I be surprised to know that?

22 **Q. Would you have any reason to doubt?**

23 A. No, I would not.

24 **Q. Okay. And it's your understanding that**
25 **a portion of those funds were used to pay for a**

1 premium price; is that correct?

2 A. Let me --

3 Q. Or a goodwill? There's a certain
4 amount of goodwill; is that correct?

5 A. Yeah. Well, I think the way I would
6 describe it is this: The Company paid roughly a
7 billion dollars. That billion dollars was for
8 the assets, generally the rate-based, other
9 assets, and a premium over-the-book value. That
10 premium over-the-book value generally would be
11 the goodwill amount. So the funding raised to
12 finance the transaction, paid for both the
13 physical assets and the goodwill asset. Does
14 that answer your question?

15 Q. Well, I'm trying to see. So the price
16 paid above the book value for the goodwill,
17 wouldn't that number be \$210 million?

18 A. It is, yes.

19 Q. And that's what appears in your
20 testimony?

21 A. Yes, that's correct.

22 Q. So if my math is correct then and the
23 purchase price is relatively consistent with the
24 table you cited to the book value of the -- the
25 utility assets would be approximately

1 **\$800 million, right?**

2 A. Approximately, right.

3 **Q. After that acquisition and merger, it's**
4 **my understanding Laclede had combined their**
5 **assets with MGE's assets; isn't that true?**

6 A. My understanding, yes.

7 **Q. And then on the liability side of the**
8 **balance sheet, isn't it also true that Laclede**
9 **had combined utility debt with MGE's debt to**
10 **produce a new combined company debt?**

11 A. When you say combined the debt, I want
12 to be sure. My understanding is the existing
13 debt remained the existing debt but came
14 together under an entity, if that's what you
15 mean.

16 **Q. True. I'm not referring to a package**
17 **refinancing or something like that.**

18 A. Okay.

19 **Q. So in this combination, it's my**
20 **understanding that an amount was recorded to**
21 **increase the common equity by \$210 million to**
22 **account for the premium in the acquisition**
23 **price; isn't that true?**

24 A. There would have been a goodwill amount
25 of about \$210 million.

1 **Q. Okay. And was that recorded to**
2 **increase common equity by \$210 million?**

3 A. Was the book entry to increase common
4 equity by \$210 million when it was pushed down?
5 I will -- I would agree with that subject to
6 check, yeah.

7 **Q. Each year isn't it true that for a**
8 **goodwill asset, there needs to be an impairment**
9 **study done, correct?**

10 A. There is, and I refer to the impairment
11 tests in my surrebuttal testimony, that's right.

12 **Q. And that's a GAAP requirement, correct?**

13 A. Correct.

14 **Q. And what is GAAP? What is that**
15 **acronym?**

16 A. Generally accepted accounting
17 principles.

18 **Q. If you're still under surrebuttal, if**
19 **you'd flip the page, generally in 7 and 9 on**
20 **those pages --**

21 A. I'm sorry. 7 through 9?

22 **Q. Yes.**

23 A. Yes, I'm there.

24 **Q. Isn't it true you discuss fungibility?**
25 **Is that how you pronounce it?**

1 A. That's how I pronounce it as well.

2 Q. Isn't it true that you discuss that
3 capital is fungible?

4 A. Yes.

5 Q. So if Laclede had invested in a new
6 utility plan, it could fund that investment with
7 a variety of things such as debt, retained
8 earnings, equity from the parent, internal cash?
9 Those would be the tools in toolbox, correct?

10 A. Generally, and let me just describe it
11 a slightly different way, but I think we're
12 saying the same thing. At any given point in
13 time. There's a pool of dollars, and that pool
14 of dollars under your scenario would be used to
15 invest in an asset. We don't know where every
16 dollar from that pool came from, we don't know
17 whether it was from operating cash flow, we
18 don't know whether it was from -- from equity
19 received, from debt received. We don't know
20 where each dollar came from. We just generally
21 know that those are the sources of those
22 dollars.

23 Q. When a utility invests in an asset such
24 as a line or something like a gas line, that
25 would, I assume, be recorded when it's put into

1 **service and rate-based, correct?**

2 A. Yes.

3 **Q. So in that sort of situation, that type**
4 **of asset would produce cash flows, correct?**

5 A. It would -- yes, once it's put into --
6 to rate base, it would produce cash flow,
7 correct.

8 **Q. Isn't it true you recognize that a**
9 **goodwill asset is never included in rate base?**

10 A. Well, I think in this case, it is not
11 included in rate base. There are other cases
12 where the premium is in fact included in rate
13 base, and it's recoverable to the extent that
14 the savings created by the merger exceed the
15 cost. But in this case, my understanding is
16 that the Company has agreed not to put the
17 acquisition premium, not to put goodwill in rate
18 base.

19 **Q. Right. And that was a part of a prior**
20 **stipulation, correct?**

21 A. Yes.

22 **Q. Is it your understanding that a company**
23 **such as Laclede would be required to do an**
24 **impairment test on utility rate base assets each**
25 **year? Is that a requirement under GAAP?**

1 A. On utility rate base assets?

2 Q. Correct.

3 A. I think from what I've seen -- and
4 again, I'm not an accountant, so I'm not going
5 to speak to accounting rules or to GAAP as it's
6 applied, but I've a seen goodwill impairment
7 tests taken on things like natural gas
8 distribution operating segments. So it may be.

9 Q. But not in this case, correct?

10 A. Here, what we've been focused on, what
11 I've been focused on is the impairment of the
12 goodwill amount.

13 Q. So not in this case, correct?

14 A. Insofar as I know, correct.

15 Q. You've testified for Ameren Missouri,
16 KCP&L on rate of return?

17 A. I have, yes.

18 Q. Do you recall that Ameren had made an
19 acquisition about ten years ago in Union
20 Electric Company?

21 A. I do, yes.

22 Q. And that did not result in a goodwill
23 asset being recorded on Ameren Missouri's
24 balance sheet. Is that your recollection?

25 A. I have no way to say one way or the

1 other.

2 Q. Meaning you don't recall?

3 A. Meaning I don't recall.

4 Q. And you testified for Great Plains
5 Energy; isn't that correct?

6 A. Yes, I did.

7 Q. And it's a proposal to acquire Westar?

8 A. In the Kansas proceeding you're talking
9 about?

10 Q. I believe so, yes, or --

11 A. It was not here, so it must have been
12 Kansas, that's correct.

13 Q. And in that proceeding, you know, you
14 would agree that Great Plains Energy had agreed
15 to keep the goodwill asset off of the books.
16 Wasn't that a condition of the proposed
17 transaction?

18 A. So when you say "off the books," are
19 you -- if your question is like in this case,
20 did the Company agree not to -- excuse me -- not
21 to seek recovery of the acquisition premium,
22 yes, that's my recollection, just as it is in
23 this case.

24 MR. SMITH: That is my question.

25 Okay. Thank you.

1 JUDGE DIPPELL: Is that all your
2 questions?

3 MR. SMITH: It is.

4 JUDGE DIPPELL: Is there
5 Cross-Examination by MIEC?

6 MR. MILLS: Yes, thank you.

7 CROSS-EXAMINATION BY MR. MILLS:

8 Q. When you recently testified in rate
9 cases for KCPL and Ameren, was there any
10 significant amount of goodwill reflected in
11 their capital structure?

12 A. I can't recall as I sit here. It was
13 not an issue for my testimony.

14 Q. You don't recall that there was or was
15 not hundreds of millions of dollars of goodwill
16 in the capital structure?

17 A. I was not -- as I said, I do not recall
18 and it was not an issue for my rate of return
19 testimony.

20 Q. So sort of tracking from the
21 acquisition when -- and I'm speaking of
22 Laclede's acquisition of MGE --

23 A. Okay.

24 Q. -- an acquisition premium was paid,
25 correct?

1 A. Yes.

2 Q. Of \$210 million?

3 A. That's right.

4 Q. And in turn, that \$210 million was
5 recorded on the books as goodwill, correct?

6 A. Yes.

7 Q. And because of the recording of that
8 goodwill on the books and included on the
9 capital structure, rates proposed in this case
10 are higher than they would have been had it not
11 been recorded on the Company's books; is that
12 correct?

13 A. No. I don't agree with that.

14 Q. You don't agree that rates are higher
15 in this case because of the inclusion of
16 goodwill?

17 A. No. I don't believe -- I think the
18 Company's -- as I say in my surrebuttal
19 testimony, the Company's capital structure is
20 appropriate. I think at 54.2 percent for the
21 many reasons I note in my capital -- excuse
22 me -- in my surrebuttal testimony that capital
23 structure is proper and putting aside -- excuse
24 me -- putting aside any questions, however many
25 I may have regarding a goodwill adjustment.

1 So if your question is, is the
2 Company's capital structure too high, is it
3 somehow creating cash flows that are too much, I
4 disagree with that.

5 **Q. In point of fact, that was not my**
6 **question at all.**

7 **My question was: Because of the**
8 **inclusion of the goodwill in the capital**
9 **structure, are rates in this case that are**
10 **proposed, are they not higher than they would be**
11 **had that amount not been included in the capital**
12 **structure?**

13 A. I don't believe so and I'll -- for this
14 reason: When I go back and I look at how the
15 Company was financed, how the acquisition was
16 financed, the proportions in which it was
17 financed, if we're going to look at how rate
18 base is financed, if we're going to look at how
19 assets are financed, if we recognize that the
20 acquisition financing was arranged through a
21 combination of long-term debt and common equity,
22 then any adjustment to the capital structure --
23 excuse me -- relating to goodwill ought to be
24 taken out in that proportion.

25 **Q. And if you weren't -- so you're saying**

1 that if you -- you're saying that if we accept
2 Mr. Gorman's recommendation that we take the
3 goodwill out of the capital structure, that
4 rates would not go down?

5 A. Oh, no. As a matter of math, I agree
6 with you. Yes. I agree with that. I'm sorry.
7 If that was your question --

8 Q. Yes.

9 A. -- I'm sorry. I missed that.

10 Q. As a matter of math, if you do not
11 include the goodwill in the capital structure,
12 rates would be lower?

13 A. Right. And boy, I hate to do this, but
14 I'm going to say something Ms. Ahern said, which
15 is all else remaining equal.

16 Q. Sure. I understood.

17 A. But yes.

18 Q. So tracking from the payment of the
19 acquisition premium to the recording of the
20 goodwill to the inclusion of the goodwill and
21 the calculation of rates in this case, because
22 of the acquisition premium being included in the
23 capital structure, rates are higher than they
24 would otherwise have been all else equal?

25 A. So be- -- again, I think I can agree

1 with your prior question, that if a -- if the
2 goodwill amount is taken out of the equity
3 portion of the capital structure and the equity
4 ratio is lower as a consequence --

5 **Q. Yes.**

6 A. -- and we hold all else equal, then
7 yes, I agree with you.

8 MR. MILLS: That's all the questions
9 I have.

10 JUDGE DIPPELL: Thank you.

11 Midwest Energy Consumers.

12 CROSS-EXAMINATION BY MR. WOODSMALL:

13 **Q. Good morning, sir.**

14 A. Good morning.

15 **Q. As I understand from your testimony,**
16 **you are a partner in ScottMadden; is that**
17 **correct?**

18 A. Yes, that's right.

19 **Q. And Ms. Ahern is an executive director;**
20 **is that correct?**

21 A. Yes, that's right.

22 **Q. What's the difference? Who is higher**
23 **on the totem pole?**

24 A. We are -- we are all equal.

25 **Q. Everybody makes the same amount?**

1 A. Well, we're not going to talk about
2 compensation, but -- but no, I think generally
3 speaking, there are partners and then there are
4 nonpartners. I am a partner. Ms. Ahern's
5 position as an executive director is a
6 nonpartner.

7 **Q. Got you. Are you her supervisor?**

8 A. No. In ScottMadden, there's -- the
9 structures are not the way they had been in our
10 prior firm. So I would not say I'm her
11 supervisor, no.

12 **Q. You're not asked to review her**
13 **testimony?**

14 A. In this case I did not review her
15 testimony, and I would only do so if asked, but
16 as a matter of practice, as a matter of course,
17 given the Company's structure, no, that's not a
18 requirement.

19 **Q. When you were at Sussex were you her**
20 **supervisor there?**

21 A. I -- I think it's generally the same
22 answer. When I was at Sussex, I was the
23 managing partner of the firm, which really meant
24 I got to do all that real fun administrative
25 stuff, but as a matter of practice, as a matter

1 of protocol, every witness's testimony is that
2 witness's testimony.

3 Q. Okay. Let's move on to some substance
4 then. Mr. Gorman characterizes goodwill as a
5 paper asset. Do you agree with that
6 characterization?

7 A. I think that's fair.

8 Q. Okay. And could Laclede and MGE
9 provide safe and adequate service even without
10 goodwill, the goodwill asset in this capital
11 structure?

12 A. I'm sorry. Is your -- there's a lot of
13 things wrapped up in that question. So --

14 Q. Let me try to break it down.

15 You referred to goodwill as a goodwill
16 asset. Do you recall using that phrase?

17 A. Yes, that's right.

18 Q. And could Laclede/MGE provide safe and
19 adequate service without the goodwill asset?

20 A. So again, if your question is goodwill
21 is a paper asset, it's not a physical asset.
22 It's the physical assets that provide safe and
23 reliable service. I assume that's what you're
24 getting to?

25 Q. Right.

1 A. And the Company's ability to continue
2 to provide safe and reliable service with those
3 physical assets of course is dependent upon its
4 ability to gain reasonable and appropriate
5 regulatory outcomes. If we assume all of that,
6 then yes, I would agree.

7 Q. Okay. And so if this paper asset, the
8 goodwill asset was included on Spire's books
9 instead of Laclede's, we would not have the
10 issue here today; is that correct?

11 A. That's probably right.

12 Q. Okay. Mr. Smith was asking some
13 questions about Westar, and I don't know, maybe
14 it was me hearing it wrong.

15 In the first iteration, Great Plains
16 was going to buy Westar and make it a
17 subsidiary; is that correct?

18 A. Correct.

19 Q. And there was an acquisition premium
20 associated with that; is that correct?

21 A. There was.

22 Q. And Great Plains agreed as part of its
23 initial request that it would keep that
24 acquisition premium at the parent company level;
25 is that correct?

1 A. That's right.

2 Q. Okay. And so we wouldn't have the
3 issue there if the goodwill was kept at the
4 parent company level; is that correct?

5 A. Right. If the accounting were such
6 that it was agreed for accounting purposes keep
7 it there, that's right.

8 Q. And I believe you testified earlier
9 that you've testified on behalf of the Great
10 Plains subsidiaries, KCP&L and GMO; is that
11 right?

12 A. Yes, that's right.

13 Q. And is it your understanding that GMO
14 was created by the Great Plains purchase of the
15 former Aquila Properties?

16 A. Yes.

17 Q. And do you know if there was an
18 acquisition premium associated with that?

19 A. I could not tell you as I sit here.

20 Q. Okay. So you don't know if the
21 acquisition premium, if it existed was kept at
22 the parent company level or at subsidiary level?

23 A. No, I couldn't tell you as I sit here.
24 Never really became an issue in any of my
25 testimony.

1 **Q. Okay. Do you recall -- even if it**
2 **wasn't an issue in your testimony, do you recall**
3 **it being an issue in the last rate cases?**

4 A. I don't recall, no.

5 MR. WOODSMALL: Okay. I have no
6 further questions. Thank you.

7 JUDGE DIPPELL: Thank you.

8 Is there anything from Environmental
9 Defense?

10 MS. KARAS: No questions, your
11 Honor.

12 JUDGE DIPPELL: Any questions from
13 the Bench for Mr. Hevert?

14 CHAIRMAN HALL: Maybe just a few.

15 QUESTIONS BY CHAIRMAN HALL:

16 **Q. Good morning.**

17 A. Good morning.

18 **Q. Do you believe that the goodwill**
19 **adjustment being advocated by Mr. Gorman in this**
20 **case is unprecedented?**

21 A. My understanding is it's unprecedented
22 in this jurisdiction. I think there may be
23 other jurisdictions where goodwill adjustments
24 had been made. I think there probably are many
25 others where it has not, and as I said earlier,

1 there are certainly jurisdictions where an
2 acquisition premium was included in a rate base,
3 there was a recovery on itself. I think in
4 terms of precedent, it goes a lot of ways, but
5 my understanding is that in Missouri, this would
6 be uncommon.

7 **Q. Were you in the hearing room when**
8 **counsel for MECG suggested some explanation for**
9 **why such an adjustment has not been made in**
10 **prior cases in this jurisdiction?**

11 A. I was, yes.

12 **Q. And how would you characterize that**
13 **description or that explanation?**

14 A. Because it really just hasn't been at
15 issue in terms of the -- the goodwill being at
16 the subsidiary level.

17 **Q. Because the parties in those cases**
18 **specifically mandated that it -- that it not be**
19 **so recorded, correct?**

20 A. Correct. There would be no recovery of
21 the goodwill either directly or indirectly as
22 there is in this case.

23 **Q. So then it really is somewhat**
24 **irrelevant that it's unprecedented, because it**
25 **just hasn't been an issue. So no one's made the**

1 request before because it's never been at issue
2 before?

3 A. No one's made the request for the
4 adjustment that Mr. Gorman has recommended. Is
5 that your point?

6 Q. Correct.

7 A. Yes. That may well be, yes, yes.

8 Q. Have you done a calculation on the
9 financial impact to the revenue requirement if
10 the Commission were to adopt Mr. Gorman's
11 suggestion on the \$210 million goodwill
12 adjustment?

13 A. I have not, and I think it would be
14 somewhat difficult to do so. We can easily say
15 what is the effect of a lower equity ratio if we
16 keep everything else constant. I think what's
17 more difficult is -- for the reasons Ms. Ahern
18 noted, is understanding what the effect on the
19 costs of capital would be as a consequence of
20 that decision. So I think there are a couple of
21 moving parts to that analysis.

22 CHAIRMAN HALL: I believe that's all
23 I have. Thank you.

24 THE WITNESS: Thank you.

25 JUDGE DIPPELL: Thank you.

1 Commissioner Rupp.

2 COMMISSIONER RUPP: Thank you.

3 QUESTIONS BY COMMISSIONER RUPP:

4 Q. Good morning.

5 A. Good morning.

6 Q. So help me remember. Goodwill can be
7 things that have an inherent value even though
8 they are not a physical asset, such as positive
9 name ID, viewpoint of the companies, how they're
10 looked in the community and things.

11 Are all those things attributable to
12 goodwill as some value?

13 A. I think that's right, and to the extent
14 that an acquirer has a view of value above the
15 net book value of the assets for whatever
16 reason, likely including the factors that you
17 just noted, that would contribute, that would
18 give rise to goodwill.

19 Q. So like if I wanted to go buy Nike, I'm
20 buying more than just the inventory and the
21 production plant. I'm buying the name and their
22 image and their -- that's why I'm paying a
23 premium?

24 A. Yes, that's right.

25 Q. I'm sorry, I'm going back to the

1 beginning here because I thought I understood a
2 few things and everybody's questions got me all
3 confused again.

4 A. Yeah, it's not a simple topic.

5 Q. So there is an inherent value of
6 goodwill and that's why people pay a premium.
7 So I guess help me from your viewpoint -- I know
8 you don't work for the Company, why would a
9 company book the goodwill in Laclede instead of
10 in Spire when they did their -- what would be a
11 possible reason for that?

12 A. You know, I wish I could answer, but,
13 again, I'm not an accountant and perhaps
14 Mr. Rasche might be able to answer that a
15 little bit better for you.

16 Q. Okay. We'll save that one for
17 Mr. Rasche.

18 So if there is a value to the goodwill
19 and there's an agreement not to include any of
20 that into rate base, how -- by including
21 goodwill in the calculations, how is that not
22 violating that agreement? Can you explain to me
23 that?

24 A. Well, we're -- first off, as you know,
25 the Company's not including goodwill in the rate

1 base and the Company is looking at the capital
2 structure that it uses to finance its assets and
3 it's looking at the -- how -- what the proper
4 mix of that capital ought to be, and in the
5 Company's discretion it's about 54, 54 percent.

6 So in my view, there is no -- there's
7 no indirect or certainly no direct recovery of
8 goodwill. The Company is simply financing its
9 assets in the way that it would in the course of
10 business, given the nature of the utility
11 operations that it provides.

12 **Q. Okay. So if the goodwill comes from**
13 **the purchases of the other companies and we're**
14 **just looking -- let's say that I wanted to do**
15 **just a Laclede capital structure and the**
16 **goodwill came from organizations outside of**
17 **Laclede. How should I handle that in your**
18 **opinion?**

19 A. I -- that's a great question. I think
20 you should handle that in large measure the way
21 we've been looking at it in some of this
22 testimony, which is to say we recognize that
23 establishing capital structure is a complicated
24 business. It depends on the individual company,
25 it depends on the assets it's financing, it

1 depends on the nature of the risks.

2 And so we have to look at measures of
3 industry practice, is the Company's capital
4 structure as it's been managed generally
5 consistent, for example, with those we see
6 elsewhere, does the Company consider things like
7 the life of its assets and the corresponding
8 life of the securities that it issues to support
9 those assets?

10 I think to me that's how we look at it.
11 And I say that because I've spent a good ten
12 years of my career managing a gas utility's
13 balance sheet, so these type of issues were very
14 real to me.

15 I think that the perspective that we
16 take when we look at whether a capital structure
17 is reasonable: Has the Company financed its
18 assets in a manner that's consistent with the
19 industry, is it consistent with the nature of
20 the operations, is it prudent in the sense that
21 there's neither too much nor too little equity,
22 is it prudent in the sense that it has properly
23 staggered maturities? There's a whole lot of
24 things that go on in terms of determining the
25 capital structure, but at the end of the day we

1 have to look at practices -- excuse me --
2 measures of industry practice as measures of
3 reasonableness.

4 Q. Okay. So the premium comes from the
5 other companies outside of Laclede if we're
6 looking at a Laclede capital structure. Is
7 there a way to tease out or to quantify the cost
8 savings?

9 Because I'm sure there's -- you know,
10 there's been savings by spreading your costs
11 over a larger group and some efficiencies and
12 things. Is there a way to tease out those cost
13 savings so as if you're not going to be charged
14 the premium, can you back out the cost savings
15 as well?

16 A. Well, my understanding is that
17 Mr. Flaherty had done an analysis of savings
18 that arose from the merger, and so that as a
19 consequence of the merger and, of course, the
20 financing that was raised to consummate the
21 merger or the transaction, those savings were
22 generated.

23 Q. And Mr. Flaherty is? When's he
24 coming? Oh, he's on Wednesday, December 12th?

25 MR. PENDERGAST: 13th.

1 COMMISSIONER RUPP: 13th.

2 BY COMMISSIONER RUPP:

3 Q. So if I dig back into Mr. Flaherty's
4 testimony, I can find a way if I was to have a
5 capital structure for Laclede and not to count
6 goodwill, I -- there would be a way in there to
7 identify the savings that would be passed only
8 to Laclede as well from --

9 A. Well, I think from Mr. Flaherty's
10 testimony you would be able to see his estimate
11 of the savings that were created by the
12 transaction. And in my view, those savings, of
13 course, were enabled by the capital that was
14 raised to be able to finance the transaction,
15 so -- and that capital, of course, relates to
16 the capital structure.

17 Q. So let's go back to the
18 10,000-foot-level view. If there's savings from
19 the merger, I have to make the assumption that
20 those savings are being passed on to Laclede and
21 to that organization as well?

22 A. I -- well, if there are savings in the
23 merger -- again, I think I'd defer to Mr. --
24 I'm doing a lot of deferring here, aren't I?
25 I'd defer to probably Mr. Loehster, but in terms

1 of how they're reflected in the cost of service.
2 But savings arising from the merger were
3 estimated being realized, and so those savings
4 have occurred.

5 Q. Okay. So how do I get my head around
6 if I'm not going to count the goodwill in my
7 capital structure, so I can't count that
8 premium, but I'm going to allow any potential
9 efficiencies and stuff to be counted, is -- how
10 do I do it either way, if I'm not going to count
11 it, I'm not going to count it or I'm going to
12 count it all? Is there a way -- I want to make
13 sure that we're not taking the juice and, you
14 know, giving away the pain.

15 A. Well, again, I think in terms of how
16 the savings are reflected in the cost of
17 service, another witness, maybe Mr. Loehster,
18 can explain that.

19 But just at a high level, we know that
20 there's a capital structure, 54 percent equity,
21 46 percent debt call it. And if your question
22 is, does that capital structure create savings,
23 are there benefits that arose from it, I think
24 the benefits that arose from it were in the
25 context of operating cost savings that were

1 enabled by the merger itself. So -- and, again,
2 that was, I understand, the topic of
3 Mr. Flaherty's testimony what those savings
4 were and how they were created by the
5 transaction.

6 Q. Okay. I still think I'm confused. So,
7 hopefully, I -- the other people -- I know I'm
8 not articulating my question. Many times we
9 have people come before us and they want to
10 enjoy the fruits of this, but, you know, not
11 have to pay for it over here, and with all the
12 different people wanting to pull this and that
13 out, I'm -- I want to make sure that if -- I
14 want to make sure I'm trying to be as fair as
15 possible and not just -- you know, trying to get
16 to a certain number and -- in that way. So
17 that's what I'm trying --

18 A. And I appreciate that. Just what I
19 would say at a very high level is that you have
20 a capital structure that's consistent with
21 industry practice, you have savings that were
22 created by the transaction. So that's what I
23 would say.

24 Q. So a 10,000-foot view in your opinion
25 is the capital structure, this is what got us

1 here, so you need to dance with those that
2 brought you rather than start -- you wouldn't
3 have this the savings if you didn't have the
4 existing capital structure?

5 A. Well, I think the -- even if we were to
6 sort of put aside the transaction, I think the
7 capital structure is reasonable. I think it's
8 consistent with industry practice. I think it's
9 a reasonable capital structure. It so happens
10 that that capital structure enabled the
11 transaction which created the savings.

12 Q. All right. Very good. Now I've got to
13 find the original questions that I had.

14 In your testimony you talked about --
15 you were talking about the economic value --
16 that equity investors -- we were talking about
17 the economic value of the goodwill and like who
18 would invest in a risk-free asset and it was
19 when you were talking about, I think,
20 Mr. Gorman's -- walk me through that again.

21 A. Sure. I think the issue -- the
22 proposition for Mr. Gorman was that you could
23 not finance goodwill with debt because goodwill
24 in and of itself produces no cash flow and
25 therefore it would not be possible to service

1 debt used to finance goodwill and therefore it
2 must have been financed with equity. That's as
3 I understand the proposition.

4 My response is really twofold. One is,
5 again, we cannot say in the context of the
6 transaction that this dollar of equity was
7 raised specifically to finance this dollar of
8 goodwill and, in fact, I think if you look at.
9 For example the prospectus that was issued prior
10 to the transaction, you'd see that the financing
11 was expected to be a mix of debt and equity.
12 And I think if you were to look at how the
13 proceeds of the acquisition debt, debt raised in
14 the context of the acquisition, the use of
15 proceeds there too, it was to fund the
16 acquisition. Not to fund rate-based, but the
17 acquisition. So that's the first thing. We
18 can't say that a dollar of equity necessarily
19 was pointed towards goodwill.

20 Secondly, if goodwill produces no
21 economic value, probably not even I would invest
22 in it. You wouldn't invest in something that
23 has no value if you can put your money in a
24 treasury bill that gives you a very low risk
25 return. So I didn't -- I didn't agree with that

1 proposition.

2 Q. Okay. I think you answered those
3 questions. Thank you, sir.

4 A. Thank you.

5 JUDGE DIPPELL: Thank you.

6 Is there further Cross-Examination
7 based on questions from the Bench from Staff?

8 MR. THOMPSON: Thank you, Judge,
9 just a few.

10 RE-CROSS-EXAMINATION BY MR. THOMPSON:

11 Q. You understand, Mr. Hevert, that as a
12 condition precedent to being permitted to
13 acquire MGE, Laclede Gas Company agreed to
14 forego any direct or indirect recovery of the
15 acquisition premium?

16 A. I understand that, yes.

17 Q. So the issue is not whether the
18 goodwill has value. The issue is whether or not
19 it's permitted to be in the capital structure;
20 wouldn't you agree?

21 A. I would agree that there should be no
22 direct or indirect consequence of goodwill in
23 the transaction, yes.

24 Q. So if the Commission were to adopt the
25 capital structure recommended by the Company

1 **rather than the capital structure recommended by**
2 **Mr. Gorman, ratepayers would pay a higher rate;**
3 **isn't that correct?**

4 A. I think we talked about this a little
5 bit ago. As a matter of math, if there's a
6 lower equity ratio, then, yes, that would be the
7 case.

8 **Q. Okay. And how is that not an indirect**
9 **recovery of that acquisition premium?**

10 A. Because I think a 47 percent equity
11 ratio is inconsistent with industry practice. I
12 don't think it's a proper capital structure and
13 I don't think that's how the Company would
14 finance itself. I don't agree. Nor do I agree
15 that when the asset -- excuse me -- when the
16 transaction was financed that equity was raised
17 specifically to fund goodwill. But in terms of
18 your math, I agree with you.

19 MR. THOMPSON: Thank you. That's
20 all my questions.

21 JUDGE DIPPELL: Is there further
22 Cross-Examination from Public Counsel?

23 MR. SMITH: Yes, very briefly.

24 RE-CROSS-EXAMINATION BY MR. SMITH:

25 **Q. You had discussed with Commissioner**

1 Rupp about the characterization of Mr. Gorman's
2 testimony and I think you characterized his
3 testimony as saying it would not be possible to
4 finance the goodwill with debt. Wasn't he
5 saying it would not be prudent?

6 A. That's fair. Yeah, I think that's
7 fair. That's right. But to be quite honest
8 with you, again, having financed --

9 Q. And that was all the question I have.
10 Thank you.

11 JUDGE DIPPELL: Thank you.

12 MIEC.

13 MR. MILLS: Yes, thank you.

14 RECROSS-EXAMINATION BY MR. MILLS:

15 Q. Is it your testimony that the capital
16 structure proposed by Mr. Gorman is so
17 unreasonable that no company would ever operate
18 using it?

19 A. That -- I don't think that's what I
20 said.

21 Q. Okay. Next question. Have you ever
22 proposed an adjustment to a capital structure in
23 a rate case?

24 A. Proposed an adjustment to a capital
25 structure? I can think of instances that are

1 unlike this case where the subject company was,
2 let's say, a division of another entity, it had
3 no capital structure of its own and therefore we
4 had to develop a capital structure.

5 So if that would fall under your
6 definition, then, yes, I suppose I would agree
7 with that.

8 **Q. Now, I believe you testified in**
9 **response to a question from Chairman Hall that**
10 **if the Commission were to make an adjustment to**
11 **the capital structure, that would have such a**
12 **profound impact on return on equity that it**
13 **shouldn't be done. Is that more or less what**
14 **you said?**

15 A. I don't -- I don't think that's what I
16 said. I think what I said was that I don't
17 think -- I think what I said is that there are
18 moving parts here.

19 And the moving part would be: If
20 you're going to have an adjustment from -- and
21 let's talk round numbers -- 54 percent to 47
22 percent equity, I don't think the cost of equity
23 would remain constant.

24 **Q. All right. Say, for example, there was**
25 **a 100, \$200 million issue with respect to costs**

1 for remediating a manufactured gas plant --

2 A. Okay.

3 Q. -- and the Commission worked to make a
4 disallowance of \$200 million. Would that also
5 have a similar impact on return on equity?

6 A. Let's -- I need a little more
7 information in your hypothetical. Was it
8 disallowed because of imprudence?

9 Q. Yes.

10 A. Okay. I don't think here in this case
11 we're talking about a 54 percent equity ratio as
12 being imprudent, so I just don't see the two as
13 being the same.

14 Q. My question wasn't whether they were
15 similar, but would they not from your point of
16 view have a similar impact on the appropriate
17 authorized return on equity if there is a -- if
18 they disallow us for any reason?

19 A. I don't think that's necessarily true.
20 I think investors understand that companies are
21 always at risk for prudence disallowances, and
22 that's why I was a little bit -- I don't think
23 your hypothetical flows from one to the other.

24 But as to a disallowance of a hundred
25 million dollars for the imprudent management of

1 an asset as opposed to a capital structure
2 that's consistent with industry practice, I do
3 think investors would see a difference between
4 those two things.

5 **Q. Have you proposed anything in this case**
6 **that would allow the Commission to make an**
7 **adjustment to the capital structure and make an**
8 **according adjustment to the return on equity?**

9 A. And is your question do I have any
10 testimony here saying, let's say, the Commission
11 decides the equity ratio should be 47 percent,
12 what then should be the cost of equity?

13 **Q. Yes.**

14 A. Oh, I haven't, but I can tell you it
15 would be higher.

16 **Q. So it's your testimony that the**
17 **Commission simply shouldn't make an adjustment**
18 **to the cost of -- to the capital structure**
19 **because that would have a big impact on return**
20 **on equity and there's been no proposal made to**
21 **address that?**

22 A. I don't -- I think that's -- you've
23 mischaracterized my testimony with that. That's
24 not my testimony.

25 My testimony is that the Company -- the

1 Company's capital structure is proper, it's
2 consistent with industry practice and in my view
3 should be allowed.

4 Q. I'm not talking about your pre-filed
5 testimony. I'm talking about your testimony in
6 response from the questions from Chairman
7 Hall --

8 A. Okay.

9 Q. -- about the impact on return of equity
10 from making a capital structure adjustment.

11 A. And what is your question?

12 Q. Is it not your testimony that based --
13 in response to his question, that the Commission
14 should not make an adjustment to the capital
15 structure aside from all the other reasons that
16 you said in your pre-filed testimony but also
17 because it would have an impact on return on
18 equity which has not been addressed in this
19 case?

20 A. No, I did not say that. What I said
21 was I don't think the Commission should make an
22 adjustment because I think the Company's capital
23 structure is prudent. If the Commission were to
24 make an adjustment, then there should be a
25 corresponding adjustment to the return on

1 equity.

2 MR. MILLS: Okay, thank you. That's
3 all I have.

4 JUDGE DIPPELL: Midwest Energy
5 Consumers.

6 MR. WOODSMALL: Yes, briefly.

7 RECROSS-EXAMINATION BY MR. WOODSMALL:

8 Q. If the Company came in with a capital
9 structure of 47 percent in this case, would you
10 say that the Company's capital structure was
11 imprudent?

12 A. If the Company had reason to believe
13 that 47 percent was the proper reason -- excuse
14 me -- the proper equity ratio, then I would
15 typically defer to the Company's discretion
16 there. But, of course, that's not the case
17 here.

18 Q. Right.

19 There were some questions from
20 Commissioner Rupp and I just want to get some
21 clarification. First off, would you agree that
22 the merger -- the acquisition, excuse me, of MGE
23 occurred in 2013?

24 A. Yes, I agree with that.

25 Q. Okay. And would you agree that there's

1 a difference between transition costs and
2 acquisition premium?

3 A. Yes.

4 Q. And what is that difference?

5 A. When you say "transition costs" -- so
6 transition costs to me are costs incurred to
7 effectuate the transaction -- excuse me -- the
8 transaction from an operational perspective.
9 They're typically one-time costs that are
10 incurred that subsequently would enable ongoing
11 operating synergies. Premium simply is that --
12 it's the amount paid in excess of book value.

13 Q. Okay. And would you agree that some
14 refer to transition costs as the costs to unlock
15 synergy savings?

16 A. I've used the term "cost to achieve,"
17 but I think it's the same thing.

18 Q. Okay. And is it your understanding
19 that some amount of transition costs have been
20 recovered from ratepayers in this case?

21 A. I could not speak to that, but I'll
22 tell you my understanding about those type of
23 costs to achieve. They're typically recovered
24 to the extent that the savings exceed costs to
25 achieve. So if that were the standard and that

1 were the case, yes, I would agree with that.

2 **Q. Okay. And would you agree that any**
3 **cost savings that have been realized since 2013,**
4 **since the acquisition, have benefited entirely**
5 **to the shareholders to this point?**

6 A. That's a really interesting question.
7 For that limited period, yes.

8 But keep in mind that when these cost
9 savings occur, they then will go on for quite a
10 period of time. So whereas perhaps in some
11 situations the Company, the shareholders may
12 have realized benefits for a couple of years,
13 ratepayers will realize benefits for many, many
14 years.

15 **Q. Right. But for the past four years,**
16 **the cost savings have been solely to the benefit**
17 **of shareholders?**

18 A. I would defer to probably Mr. Loehster
19 on that, but just as a general proposition,
20 again, in my experience if -- if there are
21 savings realized between cases, then often they
22 would go to the shareholders, but in the long
23 run, the order of -- it's significantly greater,
24 the benefits, that over time go to the
25 ratepayers.

1 **Q. And if cost savings increase between**
2 **rate cases, so let's say there's further cost**
3 **savings following this case, those will go**
4 **entirely to the shareholders until the next**
5 **case; is that correct?**

6 A. I think that's the case in any
7 construct when there's regulatory lack.

8 **Q. Thank you.**

9 A. And then, conversely, if costs go up,
10 the shareholders eat those.

11 MR. WOODSMALL: No further
12 questions. Thank you.

13 JUDGE DIPPELL: Thank you.

14 Anything from the Environmental Defense
15 Fund?

16 MS. KARAS: No questions, your
17 Honor.

18 JUDGE DIPPELL: Thank you.

19 Is there Redirect from Spire?

20 MR. PENDERGAST: Yes. Thank you

21 REDIRECT EXAMINATION BY MR. PENDERGAST:

22 **Q. Mr. Hevert, you were asked a number of**
23 **questions about why the goodwill is on Laclede**
24 **Gas Company's books rather than its parent**
25 **company's books. Do you recall those questions?**

1 A. I do.

2 Q. Do you know who bought MGE, the assets
3 of MGE? Was it Laclede Gas Company or was it
4 its parent company?

5 A. The transaction was MO Laclede.

6 Q. Okay. And since it was Laclede that
7 purchased the assets of MGE. Would you expect
8 any goodwill associated with it to be on Laclede
9 Gas Company's books?

10 A. At Laclede Gas Company's books, yes.

11 Q. Okay. Just so we're all clear on what
12 impact this acquisition had on Laclede's capital
13 structure, first of all, as you said, the
14 goodwill or the premium that was paid to acquire
15 those assets has been excluded from rate base?

16 A. Yes.

17 Q. A couple hundred million dollars, it's
18 sitting over here (gesturing) and Laclede is not
19 earning anything on that?

20 A. Correct.

21 Q. Okay. The transaction costs that were
22 incurred by Laclede Gas to make this acquisition
23 happen, are they also not reflected in rates?

24 A. Yes, that's my understanding.

25 Q. And what may be reflected in rates will

1 be some transition costs, to the extent the
2 Commission allows them, that, if you know, are
3 relatively small in comparison?

4 A. That would be my experience, that's
5 right.

6 Q. Okay. And in exchange for the Company
7 paying the entire premium, paying all the
8 transaction costs and getting back a small
9 amount of transition costs, to the extent that
10 we have quantified tens of millions of dollars
11 of cost of service reductions in this case that
12 are going to be passed through to customers, has
13 the premium that's not being earned on allowed
14 those cost savings to be achieved?

15 MR. MILLS: I object. That's a
16 leading question.

17 BY MR. PENDERGAST:

18 Q. What is the impact of the premium that
19 was paid and that is being absorbed by the
20 Company on savings that have been achieved by
21 customers?

22 A. Well, as I think I say in my testimony,
23 in my surrebuttal testimony, it was the
24 financing that was -- that was arranged. It was
25 the financing that enabled the acquisition,

1 including the goodwill that enabled those
2 savings. So the financing that arose and the
3 goodwill that arose from the transaction was
4 enabled by all the financing that was raised,
5 including the equity, including the debt. So
6 that is what enabled those savings that you just
7 mentioned.

8 Q. Okay. And in terms of the acquisition
9 and the premiums impact on the Company's capital
10 structure, can you tell me generally what equity
11 component Laclede had prior to this acquisition
12 activity?

13 A. I -- I couldn't tell you exactly as I
14 sit here. I'm sorry.

15 Q. Okay. So you wouldn't know whether it
16 was in the mid 50s for years before this
17 acquisition activity started?

18 MR. MILLS: Objection. That's
19 leading.

20 THE WITNESS: Well, what I --

21 JUDGE DIPPELL: Mr. --

22 THE WITNESS: Oh, I'm sorry.

23 JUDGE DIPPELL: Objection sustained.

24 Do you have a nonleading question?

25 MR. PENDERGAST: Yeah.

1 BY MR. PENDERGAST:

2 Q. If you could turn to page 6.

3 A. (Witness complying.)

4 Q. In there you have the table "The Source
5 of Funds."

6 A. Yes.

7 Q. Okay. And if I look at that table, was
8 a little bit more debt issued than equity in
9 order to go ahead and acquire MGE?

10 A. Yes. Well, about 5 million more.

11 Q. Okay. So what would that tell you as
12 far as whether this acquisition had an impact on
13 increasing the equity ratio for Laclede Gas
14 Company?

15 A. It would tell me that slightly more
16 debt was raised than equity. So at the margin,
17 it would not have increased the equity ratio.

18 Q. Okay. And on the first mortgage bonds,
19 do you know what the cost of those first
20 mortgage bonds were and how they compared to the
21 existing debt that Laclede had at the time?

22 A. Just bear with me one minute.

23 (Reviewing document.)

24 So the yield on the first mortgage
25 debt, the coupon, anyway, was in the range of,

1 say, 3.7 percent to 4.8 percent across the three
2 tranches.

3 Q. Okay. And, to your knowledge, is
4 Mr. Gorman proposing to somehow exclude that
5 low-cost debt from the capital structure in this
6 case?

7 A. No, he's not.

8 Q. Okay. In fact, is it true that what
9 he's doing is just assigning all of the goodwill
10 to common stock, to equity, and none of the
11 debt?

12 A. Yes.

13 Q. Okay. Do you believe that's
14 appropriate?

15 A. No. As I say in my testimony, when the
16 acquisition occurred, the financing noted in
17 that table was raised to acquire all the assets,
18 both physical and intangible, the rate base and
19 the goodwill, and it was raised in those
20 proportions to acquire all of those assets
21 without being able to assign portions of the
22 financing to either the rate base or the
23 goodwill.

24 Q. You were asked a number of questions
25 about whether or not absent this goodwill

1 adjustment you would see an adverse effect on
2 the cost of capital for the Company. Do you
3 recall those questions?

4 A. I do, yes.

5 Q. And whether or not having an impact on
6 cost of capital was prohibited by the
7 stipulation and agreement?

8 A. Yes.

9 Q. Okay. Can you tell me what's your
10 opinion of allocating all of the goodwill to
11 equity and excluding equity has on rates?

12 A. Well, that was the second part of the
13 pieces that move. If you were to reduce the
14 equity ratio by seven percentage points from,
15 again, say, 54 to 47 percent, two things would
16 happen. One is you increase financial risk.
17 And financial risk simply means that there's
18 more debt leverage in the capital structure and
19 increased financial risk means increased costs
20 of capital, typically on both the debt and the
21 equity side.

22 Now, there certainly are methods and
23 models that have been used to estimate what that
24 cost would be, but I think it's fair to say that
25 the effect would be to increase the cost of

1 equity simply because of the additional
2 financial leverage in the capital structure.

3 The reason is that when you add
4 leverage, it tends to effectively concentrate
5 business risk on the equity owners. You have a
6 certain amount of business risk out there and
7 now a lot more of it's taken on by the equity
8 owners because debt holders are protected to
9 some extent from business risk simply by the
10 fact that there's a contractual obligation to
11 pay them first and often they are secured by
12 other means.

13 Second, there's an element of increased
14 regulatory risk. So if you were to make a seven
15 percentage point change to go from an equity
16 ratio that's within the range of those we see
17 elsewhere to an equity ratio that is below the
18 Company's peers, in my view both sides, both
19 equity and debt investors, would see increased
20 risk.

21 Now, we know that's the case when we
22 look to as example for Moody's that assigns
23 57 percent of its credit ratings to the nature
24 of regulation. For debt -- excuse me. For
25 equity investors, that additional uncertainty

1 would create an additional risk. So I think we
2 would see increase of costs of capital, plural,
3 both debt and equity, for a variety of reasons.

4 **Q. And you said that as a matter of simple**
5 **math that if you go ahead and reduce the equity**
6 **component as proposed by Mr. Gorman, that that**
7 **would lower rates; is that correct?**

8 A. That's right, as a matter of math.

9 **Q. Okay. And in lowering rates, were you**
10 **suggesting that was an appropriate result?**

11 A. No. It simply was, again, a matter of
12 math. I don't think that math at the end of the
13 day would hold for the reasons we just
14 discussed. I don't think we could hold constant
15 the costs of capital, so I don't believe those
16 savings would accrue, as suggested by a
17 question, aimed at keeping everything else
18 constant.

19 **Q. And do you have any opinion on whether**
20 **allocating nothing but equity to this goodwill**
21 **is consistent with the stipulation and**
22 **agreements requirement that these acquisitions**
23 **not have impact on rates?**

24 A. Well, it seems that to me -- again, I'm
25 not an attorney, but my plain reading would be

1 that if the intent -- if the parties' intent was
2 for the transaction not to have an effect on
3 rate and if the Company's capital structure as
4 proposed is reasonable and consistent with
5 industry practice, then making an adjustment
6 would have an effect on rates re- -- owing to
7 the transaction.

8 MR. PENDERGAST: Thank you very
9 much. I have no further questions.

10 JUDGE DIPPELL: Thank you. Seeing
11 no further questions then for Mr. Hevert, you
12 may step down.

13 THE WITNESS: Thank you.

14 (Witness excused at a 12:14 p.m.)

15 MR. THOMPSON: Judge, before you go
16 off the record, if I may, you had asked a
17 question at the beginning of the proceedings
18 today about Exhibit 56.

19 JUDGE DIPPELL: Yes.

20 MR. THOMPSON: And I am told by Miss
21 Payne that Staff has no objection.

22 JUDGE DIPPELL: Okay. Would there
23 be any objection to Exhibit No. 56 which was
24 offered on Friday?

25 (No response.)

1 JUDGE DIPPELL: Then seeing none, I
2 will admit No. 56.

3 (SPIRE EXHIBIT NO. 56 RECEIVED INTO
4 EVIDENCE.)

5 JUDGE DIPPELL: Thank you for that
6 information, Mr. Thompson.

7 MR. THOMPSON: Thank you, Judge.

8 MR. SMITH: And, Judge, you had also
9 asked counsel a question about Mrs. Autt's
10 testimony and I was able to find out that the
11 correction was just a formatting correction,
12 added a cover page to her testimony and added a
13 designation of the schedules so it was more
14 clearly labeled.

15 JUDGE DIPPELL: All right. So when
16 we get to that, we will go off that most
17 recently filed exhibit.

18 MR. SMITH: Yes.

19 JUDGE DIPPELL: All right.

20 Well, it is lunchtime, so we will take
21 a lunch break. We are moving very slowly this
22 morning. These are some big issues that need to
23 be covered thoroughly, but just keep that in
24 mind as you prepare your questioning for later
25 today and the other witnesses.

1 We can go ahead and take a lunch break
2 until 1:30.

3 MR. THOMPSON: Thank you, Judge.

4 MR. SMITH: Thank you, Judge.

5 (Recess taken from 12:15 p.m.
6 to 1:30 p.m.)

7 JUDGE DIPPELL: Let's go back on the
8 record. Okay, we're back on the record after
9 our lunch break and we, I believe, are ready for
10 the next Spire witness.

11 MR. PENDERGAST: Thank you, your
12 Honor. The Company would call Steven P. Rasche
13 to the stand.

14 (Witness sworn.)

15 THE WITNESS: I do.

16 JUDGE DIPPELL: Okay. Go ahead,
17 Mr. Pendergast.

18 MR. PENDERGAST: Thank you.

19 STEVEN P. RASCHE testified as follows:

20 DIRECT EXAMINATION BY MR. PENDERGAST:

21 **Q. Good afternoon, Mr. Rasche.**

22 A. Good afternoon.

23 **Q. Are you the same Steven P. Rasche which**
24 **has previously been caused to be filed in this**
25 **proceedings surrebuttal testimony that has been**

1 marked as Exhibit 37?

2 A. Yes, I am.

3 Q. Do you have any corrections to make to
4 that testimony?

5 A. No, I do not.

6 Q. If I were to ask you the same questions
7 today that appear in your direct -- or your
8 surrebuttal testimony, would your answers be the
9 same?

10 A. Yes, they would.

11 Q. And are those answers true and correct
12 to the best of your knowledge?

13 A. Yes, sir.

14 MR. PENDERGAST: At this time I
15 would offer Mr. Rasche's surrebuttal testimony
16 into evidence and would tender him for
17 Cross-Examination.

18 JUDGE DIPPELL: Is there any
19 objection to the Exhibit No. 37?

20 (No response.)

21 JUDGE DIPPELL: Seeing no objection,
22 I will enter that into evidence.

23 (SPIRE EXHIBIT NO. 37 RECEIVED INTO
24 EVIDENCE.)

25 JUDGE DIPPELL: And we can begin

1 with Cross-Examination by Staff.

2 MR. THOMPSON: No questions. Thank
3 you, Judge.

4 JUDGE DIPPELL: Public Counsel.

5 MR. SMITH: Yes.

6 CROSS-EXAMINATION BY MR. SMITH:

7 **Q. Good afternoon, Mr. Rasche.**

8 A. Good afternoon.

9 **Q. Are you a shareholder of Spire**
10 **Missouri's parent or Spire Inc.?**

11 A. Yes, I am a shareholder, as are most
12 all of our employees and many of our customers.

13 **Q. And your current title is a CFO or the**
14 **executive vice president?**

15 A. I have both titles. I generally refer
16 to myself as the CFO.

17 **Q. What is your understanding of the net**
18 **income for 2016 of Spire Inc.? What is that**
19 **number?**

20 A. The net income for 2016 for Spire Inc.?
21 I can remember the number in earnings per share,
22 but I can't give you the dollar amount because,
23 as you can imagine, I've had eight quarters'
24 worth of performance since then and I can only
25 keep certain numbers in my brain. I could

1 clearly look it up. It's -- \$3.42 per share was
2 the Spire Inc. consolidated earnings per share
3 for that year.

4 **Q. Does \$144.2 million sound correct?**

5 A. It sounds familiar, but, again, without
6 being able to reference anything, I couldn't
7 verify it or not.

8 **Q. And you said there were eight quarters**
9 **in between. So November 2017 earnings were**
10 **recently reported; isn't that correct?**

11 A. Um-hum.

12 **Q. And isn't it true that the net income**
13 **at that time was \$161.6 million?**

14 A. Yes, it was.

15 MR. SMITH: Okay. Thank you. No
16 further questions.

17 JUDGE DIPPELL: Thank you.
18 Anything from MIEC?

19 MR. MILLS: No questions.

20 JUDGE DIPPELL: Midwest Energy?

21 MR. WOODSMALL: No questions.

22 JUDGE DIPPELL: Environmental
23 Defense?

24 MS. KARAS: No questions.

25 JUDGE DIPPELL: Questions from the

1 Bench?

2 CHAIRMAN HALL: No questions.

3 COMMISSIONER KENNEY: No questions.

4 JUDGE DIPPELL: Is there any

5 Redirect?

6 REDIRECT EXAMINATION MR. PENDERGAST:

7 Q. The only Redirect I had -- we had a
8 number of questions about Exhibit 57 and I think
9 we've pointed to Mr. Rasche as somebody who
10 could reveal who the peer companies were and I
11 thought we'd give him an opportunity to go ahead
12 and do that?

13 JUDGE DIPPELL: Okay. Mr. Rasche,
14 can you answer that question about the Exhibit
15 No. 57? There's a dark gray line -- or a gray
16 line.

17 THE WITNESS: This (indicating to
18 document), right?

19 JUDGE DIPPELL: Yes. Can you
20 identify the companies that were the peer
21 companies.

22 THE WITNESS: Yes, I can.

23 This was a standard analysis that we
24 perform on a monthly basis and look at it in
25 detail on a quarterly basis, comparing our

1 performance from a share price perspective
2 against the broader market which would be the
3 S&P 500 which is the dark blue line and then
4 also our peer set.

5 Our peer set which we also use to
6 benchmark operating performance, compensation
7 and other issues has consisted of the following:
8 South Jersey Industries, New Jersey Resources,
9 Northwest Natural, WGL, Southwest Gas --

10 MR. WOODSMALL: Hold on. I'm sorry.

11 THE WITNESS: Northwest Natural...

12 JUDGE DIPPELL: If you can please go
13 a little slower.

14 MR. WOODSMALL: Yeah.

15 THE WITNESS: Southwest Gas, Atmos,
16 Black Hills, Alliant, NiSource, Northwestern,
17 ONE Gas, Vectren and Avista.

18 And these -- that group is the sub- --
19 is the set of either LDCs, pure LDCs or largely
20 gas-focused utilities that would -- that we
21 benchmark ourselves against for many operational
22 and also financial and market metrics. So it's
23 a standard performance.

24 And this analysis compares straight up
25 the shared performance for those peers as a

1 group against us in the market, and as you can
2 see and I think it was outlined in earlier
3 testimony, that our performance, even though our
4 shares have been -- increased dramatically, as
5 have most of the shares in each of your 401(k)
6 plans or 403(b) plans, our performance against
7 our peer set which is whom we not only compete
8 with for talent, but we compete with in the
9 investment market for both debt and equity
10 investment, our performance is 2700 basis points
11 below that peer set for that period. That's 27
12 full percentage points below, and it -- the
13 purpose of this -- and we look at this on a
14 routine basis to make sure that we understand
15 what's going on in the market and to the extent
16 that we can address any under-performance or can
17 explain any over-performance -- and you can see
18 there isn't much of a time period where we're
19 over-performing except for a few brief periods
20 in late 2013 and early 2014 -- so that we can
21 refine our message because ultimately our
22 communication to the capital markets is
23 important in our raising of capital at all
24 levels of the stat, whether that be at the Spire
25 Inc. level where -- it's the only place we issue

1 equity because that's the most cost effective
2 way to raise equity, but also debt raises which
3 happen not only at Spire Inc., but also at Spire
4 Missouri including our \$170 million offering
5 that we announced earlier and funded in
6 September this year. Spire Alabama, we're
7 actually in the process of completing a
8 \$75 million offering there. Half of that was
9 funded on December 1st.

10 JUDGE DIPPELL: Thank you.

11 BY MR. PENDERGAST:

12 **Q. Thank you. And was this Exhibit 57**
13 **prepared by you or under your supervision?**

14 A. It was prepared under my supervision.

15 **Q. Thank you.**

16 MR. PENDERGAST: At this time I
17 would offer Exhibit 57 into evidence, and I have
18 no further questions for Mr. Rasche.

19 JUDGE DIPPELL: Okay. I'm just
20 going to give a little caveat before I ask for
21 objections, and that is I'm going to allow you
22 all to do Cross-Examination based on those --
23 the information that we just heard. But at this
24 time would there be any objection to Exhibit 57?

25 (No response.)

1 JUDGE DIPPELL: Seeing none, then I
2 will admit that.

3 (SPIRE EXHIBIT NO. 57 RECEIVED INTO
4 EVIDENCE.)

5 JUDGE DIPPELL: And I'm going to let
6 you all have an opportunity to Cross based on
7 that testimony.

8 Is there anything from Staff?

9 RE-CROSS-EXAMINATION BY MR. THOMPSON:

10 **Q. What happened at the end of 2015,**
11 **Mr. Rasche? Looks to me based on this graph**
12 **that Spire was more or less tracking the peer**
13 **group until the end of 2015 when Spire's share**
14 **price plummeted and that of the peer group rose**
15 **and it hasn't caught up again.**

16 **A. Actually, if you look in that time**
17 **frame, everybody's shares plummeted. Ours**
18 **plummeted a little bit more.**

19 In fact, if you go to the point where
20 they do drop, I would say that the percentage
21 performance between the two was within three
22 percentage points over a three-year period,
23 which in my mind would not be statistically
24 significant. And you can see that we, the stock
25 market overall, and our peer set all dropped.

1 I believe that was -- as was mentioned
2 by a couple of the other witnesses today, the
3 stock market and the debt markets are influenced
4 by actions by the market overall, by the
5 Treasury Department and also by actions outside
6 of the United States. And I don't specifically
7 recall what the action was in that time period,
8 but I can tell you that the consistent movement
9 of all three tells me that it was probably
10 something internationally because, if you see,
11 the market overall dropped fairly significantly
12 and in a time of duress, think of North Korea or
13 other things outside of the U.S., including the
14 Brexit vote, which may be what this is,
15 utilities are viewed as a defensive stock and
16 therefore usually get more than their share of
17 interest and investment as a place to put money
18 in a relatively safe fashion.

19 **Q. If you know, when was the Alagasco**
20 **acquisition?**

21 A. We closed the Alagasco acquisition on
22 Labor Day 2014, so well before the time period
23 you're pointing out.

24 **Q. Thank you.**

25 MR. THOMPSON: No further questions.

1 JUDGE DIPPELL: Anything from Public
2 Counsel?

3 MR. SMITH: No questions.

4 JUDGE DIPPELL: MIEC?

5 RECROSS-EXAMINATION BY MR. MILLS:

6 Q. So that what you have established as a
7 peer group here is not the same as the proxy
8 group that Ms. Ahern used; is that correct?

9 A. I'm sorry, the proxy group that...

10 Q. Ms. Ahern used in your return on equity
11 analysis.

12 A. It would be not exactly the same,
13 however, there would be many utilities that
14 would be consistent between the groups.

15 Q. But her group has utilities that yours
16 does not and yours has some that hers does not;
17 is that correct?

18 A. I would suspect so, but I don't
19 specifically know all the companies that were in
20 her peer group.

21 Q. And if you had, for example, run this
22 analysis a month ago, it would probably show
23 that you were noticeably above the S&P 500; is
24 that correct?

25 A. (Reviewing document.)

1 Actually, you have to go back about
2 three months, and you can see that we've tracked
3 with the S&P fairly closely.

4 And, again, you know, those differences
5 over a five-year period are probably not
6 statistically significant, the point of this
7 chart being the delta from the gray line rather
8 than the delta from the orange line.

9 **Q. And when you run these analyses, do you**
10 **sometimes put trend lines to these marks?**

11 A. We do analyze them a number of ways,
12 yes.

13 **Q. And if you were to do it -- from**
14 **looking at this, it appears to me, and correct**
15 **me if I'm wrong, that if you were to do a trend**
16 **line for both Spire and the S&P 500, those lines**
17 **would be very, very close to each other just at**
18 **the end.**

19 A. Actually, I would say if you took the
20 trend line from the date on which we filed the
21 Missouri rate case, the trend line for us would
22 be down and the market would be up. And the
23 reason for that is the risk associated with a
24 rate case, especially in a jurisdiction where,
25 oh, 60 percent of our earnings are driven.

1 **Q. But over the five-year period that this**
2 **graph depicts, they would be fairly similar?**

3 A. Well, by definition if you would draw a
4 trend line over a five-year period, if the
5 beginning point and the end point were exactly
6 the same, the trend line would be exactly the
7 same. But the meaning of trend lines is looking
8 at shorter periods and trying to predict where
9 that performance is going in the future rather
10 than using a base in the past.

11 **Q. And if you'd looked at this and stopped**
12 **your analysis about halfway through 2015, in**
13 **fact Spire would probably -- at least for a**
14 **brief period of time, would have been above the**
15 **peer groups, correct?**

16 A. Um... I can do that mentally in my
17 head. I'm not sure whether we'd be above the
18 peer group for any time period from the start
19 change which really started about the end of
20 2015, so I think it would still show that we
21 would have underperformed our peers.

22 **Q. But there are times in here in which**
23 **the orange line is higher than the gray line,**
24 **which would indicate that you were at that point**
25 **outperforming the peer group?**

1 A. You are looking at the same information
2 I have and I see one brief period of time where
3 the orange line is above the gray line during
4 the entire analysis.

5 **Q. And are you familiar with the criteria**
6 **that Ms. Ahern and Mr. Gorman used to select**
7 **their proxy group for purposes of determining**
8 **return on equity?**

9 A. I read their testimony. I can't speak
10 to their methodology, but it's consistent with
11 what I would have expected.

12 **Q. Do you know why neither of them**
13 **included a number of the companies in their**
14 **proxy groups that you did not include in your --**
15 **that you did include in your proxy group?**

16 A. No. You'd have to ask them directly on
17 that.

18 **Q. Okay.**

19 MR. MILLS: No further questions.

20 JUDGE DIPPELL: Thank you.

21 Midwest Energy Consumers?

22 MR. WOODSMALL: Very briefly.

23 RE-CROSS-EXAMINATION BY MR. WOODSMALL:

24 **Q. You weren't here, I know, but there**
25 **were questions asked of Public Counsel witness**

1 **Chuck Hyneman the first day of the hearing in**
2 **which he provided stock price information for**
3 **the Dow Jones Industrial Average and the Dow**
4 **Jones Utility Average. Are you aware of that**
5 **testimony?**

6 A. I am not.

7 **Q. But just my point, the Dow Jones**
8 **Industrial Average and the S&P 500 are different**
9 **metrics; is that correct?**

10 A. Um-hum.

11 **Q. Is that a yes?**

12 A. Yes. Yes, they are.

13 **Q. And it wouldn't surprise you if both**
14 **pieces of testimony were accurate? They're not**
15 **in conflict since they're different metrics; is**
16 **that --**

17 A. They are different metrics. The Dow is
18 a much smaller sample of companies than the
19 S&P 500 and we think it's a better reflective
20 overall view of market active versus than any of
21 the Dows.

22 **Q. And the Dow Jones Utility Average is a**
23 **different metric than your self-filled peer**
24 **group; is that correct?**

25 A. Yes, it would include a lot of very

1 large electric utilities, which we don't believe
2 are appropriate comparators for our performance
3 given our mix of business.

4 Q. Okay.

5 MR. WOODSMALL: No further
6 questions. Thank you.

7 JUDGE DIPPELL: And anything from
8 the Environmental Defense Fund?

9 MS. KARAS: No questions, your
10 Honor.

11 JUDGE DIPPELL: All right. Is there
12 any further Redirect based on --

13 MR. PENDERGAST: No, your Honor.

14 JUDGE DIPPELL: All right. Thank
15 you for indulging me on that.

16 Mr. Rasche, I believe that completes
17 your testimony for now and you may step down.

18 THE WITNESS: Thank you.

19 JUDGE DIPPELL: Or I believe that
20 completes your testimony completely.

21 (Witness excused at 1:46 p.m.)

22 JUDGE DIPPELL: So we're ready for
23 the next Spire witness?

24 MR. FISCHER: Yes. Glenn Buck.

25 (Witness sworn.)

1 THE WITNESS: I do.

2 JUDGE DIPPELL: Thank you.

3 Go ahead, Mr. Fischer.

4 MR. FISCHER: Thank you.

5 GLENN BUCK testified as follows:

6 DIRECT EXAMINATION BY MR. FISCHER:

7 Q. Please state your name and address for
8 the record.

9 A. My name is Glenn Buck. My address --
10 business address is 700 Market, St. Louis,
11 Missouri, 63101.

12 Q. Are you the same Glenn Buck that has
13 cause to be filed in this case Direct testimony
14 which has been marked as Exhibit 19, Rebuttal
15 testimony that's been marked as Exhibit 20,
16 Surrebuttal that's been marked as Exhibit 21 and
17 True-Up Direct which has been marked as 22?

18 A. Yes, I am.

19 Q. Do you have any changes or corrections
20 that should be made to any of those testimonies?

21 A. A few. They're all grammatical and,
22 frankly, are not significant, but the first
23 one's are in Rebuttal on page 3, line 8, the
24 word "refunding" should be "refunded."

25 Q. What's your next one?

1 A. On page 6, line 20, the word "combine"
2 should be "combined."

3 **Q. Okay.**

4 A. On line 22, there's a superfluous
5 period at the end of the sentence.

6 **Q. Okay.**

7 A. On page 11, line 1, you need to add a
8 semicolon after the term "20 years." So it
9 would read "20 years;."

10 **Q. Okay.**

11 A. On line 8 of that same page, please add
12 a space between the word "item" and the number
13 "4."

14 **Q. Any others?**

15 A. Two left. Page 13, line 16, add the
16 word "make" after "likely." It's supposed to
17 say "likely make."

18 And then, finally, in my Surrebuttal on
19 page 9, line 12, the word "witness" should be
20 replaced with the word "witnesses."

21 **Q. If I were to ask you the questions that**
22 **are contained in your various testimonies today,**
23 **would your answers still be the same and are**
24 **they accurate to the best of your knowledge and**
25 **information and belief?**

1 A. Yes, they are.

2 MR. FISCHER: Judge, Mr. Buck is
3 going to be appearing on several issues, but he
4 does address the capital structure issue in this
5 area, so at this time I would tender the witness
6 for Cross-Examination.

7 JUDGE DIPPELL: Thank you. Is there
8 Cross-Examination by Staff?

9 MR. THOMPSON: No thank you, Judge.

10 JUDGE DIPPELL: Public Counsel?

11 MR. SMITH: Yes, briefly.

12 CROSS-EXAMINATION BY MR. SMITH:

13 **Q. Does Laclede or MGE anticipate funding**
14 **gas inventories with short-term debt going**
15 **forward?**

16 A. I don't think -- actually, I don't
17 really think we're funding it with short-term
18 debt currently. So the answer would be: You
19 never know what's going to happen in the future,
20 but my anticipation would be no.

21 **Q. Now, you say that the Company is in**
22 **financing with short-term debt currently. Is**
23 **that because it was refinanced to long-term**
24 **debt?**

25 A. No. I mean we've been managing our

1 debt, both short-term and long-term, based on
2 cash available to us, and for the long-term debt
3 that we've got out there -- or the short-term
4 debt that we've got out there has been largely
5 funding other short-term assets besides the
6 inventories.

7 Which is why if you look at my Schedule
8 Surrebuttal -- I mean Rebuttal Schedules AWB1,
9 it shows we compared our short-term debt
10 averages compared to other short-term assets and
11 the short-term assets were higher than that with
12 the funded inventories.

13 **Q. In the past has the Company funded gas**
14 **inventories with short-term debt?**

15 A. Yes, we have.

16 **Q. Thank you.**

17 MR. SMITH: No further questions.

18 JUDGE DIPPELL: MIEC?

19 MR. MILLS: No questions.

20 JUDGE DIPPELL: Midwest Energy?

21 MR. WOODSMALL: No questions.

22 JUDGE DIPPELL: Environmental

23 Defense?

24 MS. KARAS: No questions, your

25 Honor.

1 JUDGE DIPPELL: Are there questions
2 from the Bench for Mr. Buck?

3 CHAIRMAN HALL: No questions.

4 COMMISSIONER KENNEY: No questions.

5 JUDGE DIPPELL: Any Redirect?

6 MR. FISCHER: Yes, briefly.

7 REDIRECT EXAMINATION BY MR. FISCHER:

8 **Q. Mr. Buck, you were asked some**
9 **questions about whether the Company uses**
10 **short-term debt to fund gas inventory?**

11 A. Yes.

12 **Q. Why doesn't Laclede or Spire Missouri**
13 **include short-term debt in the capital**
14 **structure?**

15 A. Well, largely because it funds, first
16 off, construction work in progress and it also
17 funds other Commission-tarrified -- or other
18 assets that are based on Commission tariff are
19 provided for at a short-term debt rate, usually
20 prime minus 2 which is the equivalent of a
21 short-term debt rate. So it only makes sense at
22 that point to finance them -- those short-term.

23 **Q. And do those items like construction**
24 **work in progress and those other tarrified items**
25 **that you mentioned exceed the short-term debt**

1 **that you might have?**

2 A. Absolutely.

3 **Q. In past cases has Laclede included**
4 **short-term debt in its capital structure?**

5 A. No, sir.

6 **Q. In past cases has -- do you know if the**
7 **Staff has included short-term debt in its**
8 **proposed capital structure?**

9 A. In recent years, no. I think if you
10 went back 15, 20 years there may have been, but
11 not recently, no, sir.

12 **Q. Do you know if the Public Counsel has**
13 **included short-term debt in its capital**
14 **structures in previous cases that you're**
15 **familiar with?**

16 A. Not as I'm aware.

17 **Q. Are you aware of any party in cases**
18 **you've been aware -- or are aware of that has**
19 **included short-term debt in the capital**
20 **structures in Laclede cases?**

21 A. It's an awful lot of cases, but to my
22 knowledge, no, sir.

23 MR. FISCHER: That's all the
24 questions I have. Thank you.

25 THE WITNESS: Thank you.

1 JUDGE DIPPELL: I believe that's all
2 for you at this time, Mr. Buck.

3 THE WITNESS: Thank you.

4 JUDGE DIPPELL: You may step down.

5 (Witness excused at 1:53 p.m.)

6 JUDGE DIPPELL: And, Mr. Fischer,
7 can I just ask if you have three more copies of
8 Exhibit 57?

9 MR. FISCHER: Oh, if we don't, we
10 can make some.

11 JUDGE DIPPELL: If you don't have
12 them here, that's fine.

13 MR. FISCHER: I do have some here,
14 Judge. I do. I've got four, actually.
15 (Tendering documents.)

16 JUDGE DIPPELL: All right. Then we
17 are ready for Staff's witness.

18 MR. THOMPSON: Judge, Staff would
19 call David Murray to the stand.

20 (Witness sworn.)

21 THE WITNESS: I do.

22 JUDGE DIPPELL: Thank you.

23 Go ahead, Mr. Thompson.

24 MR. THOMPSON: Thank you, Judge.

25

1 DAVID MURRAY testified as follows:

2 DIRECT EXAMINATION BY MR. THOMPSON:

3 Q. State your name, please.

4 A. David Murray, last name spelled
5 M-U-R-R-A-Y.

6 Q. How are you employed, Mr. Murray?

7 A. I'm employed as a Utility Regulatory
8 Manager in the Financial Analysis Unit in the
9 Operational Analysis Department.

10 Q. And are you the same David Murray that
11 prepared or caused to be prepared several pieces
12 of testimony, first of all, a contribution to
13 Staff's revenue requirement class cost -- or
14 Cost of Service Report 204 Confidential, 205
15 Nonconfidential?

16 A. Yes.

17 Q. And then Rebuttal testimony 221
18 Confidential, 222 Nonconfidential?

19 A. Yes.

20 Q. And Surrebuttal testimony 264
21 Confidential, 265 Nonconfidential?

22 A. Yes.

23 Q. And do you have any corrections to
24 those pieces of testimony?

25 A. I do have a few corrections. On

1 page 7 -- and this is on the Staff Cost of
2 Service Report.

3 **Q. Yes, sir.**

4 A. Page 7, line 20, it indicates "6.41 to
5 6.65 percent." It should be "6.38 to 6.62
6 percent" which is consistent with the table on
7 page 8.

8 JUDGE DIPPELL: Can you re- -- hang
9 on, Mr. Murray. I was trying to catch up. So
10 page 7, line 20 is what you said?

11 THE WITNESS: Yes.

12 JUDGE DIPPELL: And could you give
13 me that change?

14 THE WITNESS: It should be
15 "6.38 percent to 6.62 percent."

16 JUDGE DIPPELL: 26 did you say?

17 THE WITNESS: 6.62.

18 JUDGE DIPPELL: 6.62. Thank you.

19 THE WITNESS: And in my Rebuttal
20 testimony, on page 1, line 24, I guess this will
21 be -- I'll leave it up to you how to put this in
22 here, but a line was left off and I don't know
23 if it will be assigned a new line number, but
24 after "the" at the end of the line, there should
25 be "Capital asset pricing model ('CAPM'), and

1 the risk premium method ('RPM') and then --

2 JUDGE DIPPELL: Start with premium
3 method?

4 THE WITNESS: Yes.

5 JUDGE DIPPELL: Start with premium
6 method and give me the --

7 THE WITNESS: Oh, I'm sorry.

8 JUDGE DIPPELL: That's okay.

9 THE WITNESS: "Premium method" and
10 then the parentheses with a quote and then an R
11 and then a P as in Pam and an M as in mom with
12 another parenthe- -- excuse me -- another quote
13 and then parentheses and then "to her."

14 JUDGE DIPPELL: To what was the last
15 thing?

16 THE WITNESS: Her, H-E-R.

17 And page 3, line 3, instead of
18 "capitol" as a, you know, physical capitol, K --
19 C-A-P-I-T-O-L, it should be C-A-P-I-T-A-L.

20 Page 7 -- this is also on Rebuttal
21 testimony, page 7, line 15, instead of "Spire
22 Incorporated issued approximately," it should
23 say "Spire Missouri issued approximately
24 40 million of short-term debt."

25 And on -- in Surrebuttal testimony on

1 page 5, line 1, before the abbreviation "ACA,"
2 "actual cost adjustment" was left out. So
3 "actual cost adjustment" before "ACA."

4 And that's it.

5 BY MR. THOMPSON:

6 Q. Does that complete your corrections,
7 Mr. Murray?

8 A. Yes.

9 Q. If I were to ask you those same
10 questions again with those corrections in mind,
11 would your answers be the same?

12 A. Yes.

13 Q. And are they true and correct to the
14 best of your knowledge and belief?

15 A. Yes.

16 MR. THOMPSON: I will not offer the
17 Revenue Requirement Cost of Service Report at
18 this time since there are more Staff witnesses
19 yet to come, but I will offer Exhibits 221, 222,
20 264, 265.

21 JUDGE DIPPELL: Would there be any
22 objection to Exhibits 221, 222, 264 and 265?

23 (No response.)

24 JUDGE DIPPELL: Seeing none, I will
25 admit those into evidence.

1 (STAFF EXHIBIT NOS. 221, 222, 264
2 and 265 RECEIVED INTO EVIDENCE.)

3 MR. THOMPSON: Thank you, Judge. I
4 will tender the witness for Cross-Examination.

5 JUDGE DIPPELL: Is there any
6 Cross-Examination from Public Counsel?

7 MR. SMITH: No questions.

8 JUDGE DIPPELL: MIEC?

9 MR. MILLS: No questions.

10 JUDGE DIPPELL: Midwest Energy
11 Consumers?

12 MR. WOODSMALL: Yes, very briefly,
13 your Honor.

14 CROSS-EXAMINATION BY MR. WOODSMALL:

15 Q. Good afternoon. Were you here when
16 Ms. Ahern testified this morning?

17 A. I was.

18 Q. And did you hear her comment that the
19 investment community will look at it as a
20 negative "a departure from a prior decision
21 making." Do you recall her saying that?

22 A. I don't recall the context.

23 Q. Okay. Anyway, is your capital
24 structure that you're representing in this case
25 a consolidated capital structure a departure

1 from the way it's been done in the past in
2 Laclede cases?

3 A. It is not.

4 Q. Okay. Is Laclede/MGE's proposed
5 capital structure a departure from the way
6 they've done it in the past?

7 A. It is.

8 Q. Can you tell me how?

9 A. They are recommending the subsidiary
10 capital structure rather than the consolidated,
11 and before -- before this case, they had
12 recommended the Laclede Group consolidated
13 capital structure for, you know, several rate
14 cases. I don't recall exactly when they started
15 doing so.

16 Q. And last question. In this case you
17 included short-term debt in the capital
18 structure. Did you include it in previous
19 cases, and if not, why did you do it here?

20 A. I did not include it in previous rate
21 cases because of the fact that, as of 2005, the
22 Company and Staff and I believe some other
23 parties agreed to recover carrying cost on gas
24 inventory balances based on the logic that
25 the -- you know, this -- it's a short-term

1 asset, so therefore a short-term rate should be
2 used for the gas inventory carrying costs flow
3 through the PGA ACA process, so it was not in
4 rate base. And with -- you know, with this
5 case, obviously, Staff is recommending it be
6 included in rate base and I believe -- you know,
7 I believe that everybody understood that the
8 logic was that the carrying charges for
9 short-term assets should be consistent with the
10 short-term rate.

11 MR. WOODSMALL: No further
12 questions. Thank you.

13 JUDGE DIPPELL: Anything from
14 Environmental Defense Fund?

15 MS. KARAS: No questions, your
16 Honor.

17 JUDGE DIPPELL: Spire?

18 MR. FISCHER: Yeah, Judge, I do have
19 some questions.

20 CROSS-EXAMINATION BY MR. FISCHER:

21 **Q. Mr. Murray, your background,**
22 **employment background credentials are all**
23 **included in appendix 1, page 42, correct?**

24 A. I don't know if I have that appendix up
25 here with me, but --

1 Q. Oh, that's all right. We've been
2 through it a number of times before. I just
3 have a few more questions related to things that
4 aren't there.

5 Prior to your employment with the
6 Commission, just for the record, were you ever
7 employed to work for any other regulatory agency
8 or financial institution?

9 A. The Department of Insurance for the
10 first five years of my working career after I
11 graduated college.

12 Q. And during that period while you were
13 with the Division of Insurance, did you do cost
14 of capital testimony for them or --

15 A. I did not. The rates weren't regulated
16 for insurance companies. Even with Workers'
17 Compensation, they had deregulated their rates
18 in 1993 I believe it was.

19 Q. And have you ever worked for any other
20 financial institution?

21 A. No, I've been with the Department of
22 Insurance and then Public Service Commission and
23 we're here, so...

24 Q. And we've been doing this for like
25 17 years, right?

1 A. Approximately so.

2 **Q. Let's -- on appendix 1, maybe without**
3 **even referring to it, is it correct that the**
4 **last natural gas rate case that you participated**
5 **in personally was the Summit Natural Gas case,**
6 **Case No. GR-2014-0086?**

7 A. I recall that -- I believe that is the
8 last case in which I personally filed direct
9 testimony, and now I just supervise other
10 employees.

11 **Q. Yeah, you've supervised other employees**
12 **recently on the Liberty case, right?**

13 A. I did.

14 MR. FISCHER: Your Honor, just to
15 short-circuit this, I would ask that the
16 Commission take official notice of the report
17 and order in the Summit Natural Gas case,
18 Case No. GR-2014-0086 which was issued on
19 October 29, 2014.

20 JUDGE DIPPELL: Would there be any
21 objection to the Commission taking official
22 notice of that report?

23 MR. WOODSMALL: I guess my only
24 question is what's the relevance?

25 MR. FISCHER: Oh, I think it will

1 become relevant. It's the last one he
2 participated in and made a recommendation. I do
3 have some -- a couple of questions about that
4 case and how it relates to this.

5 MR. WOODSMALL: Well, assuming he
6 establishes some relevance, probably not, no.

7 JUDGE DIPPELL: Well, I will let you
8 go ahead and question the witness, Mr. Fischer,
9 and then I'll rule on the admittance.

10 MR. FISCHER: Okay.

11 BY MR. SMITH:

12 Q. Mr. Murray, I'd like to show you a
13 copy of that report and I'm going to refer to a
14 couple things here.

15 JUDGE DIPPELL: And just to keep it
16 straight, I'm going to go ahead and mark that --
17 give that an exhibit number as 58.

18 MR. FISCHER: Okay. I don't have
19 enough copies for --

20 BY MR. FISCHER:

21 Q. Let's just ask you to refer to page 36
22 of that report and order where the parties
23 have -- or where the Commission lays out the
24 parties' positions.

25 A. I'm there.

1 Q. Okay. Let's look at the -- at -- first
2 at the capital structure issue on page 36. It
3 indicates that Staff had suggested a capital
4 structure of 60 percent debt and 40 percent
5 equity in this case.

6 A. That is correct.

7 Q. And then Summit Natural Gas at that
8 time was advocating the use of a 43 percent debt
9 and a 57 percent equity capital structure; is
10 that right?

11 A. Yes.

12 Q. Now, the Commission did not adopt
13 Staff's proposed capital structure in that case;
14 is that true?

15 A. It do not.

16 Q. It adopted a 57 percent equity ratio
17 that was proposed by Summit?

18 A. That's correct.

19 Q. Let's look at page 37.

20 MR. THOMPSON: Judge, I'm going to
21 join in Mr. Woodsmall's objection because
22 there's certainly been no showing of relevance
23 so far.

24 JUDGE DIPPELL: All right, that will
25 be pending as well.

1 MR. THOMPSON: Thank you.

2 BY MR. FISCHER:

3 Q. The Commission on page 37 of the report
4 and order, it begins to discuss the capital
5 structure issue that you testified about and it
6 indicates that the Commission is setting
7 Southern Missouri Natural Gas and Missouri's
8 capital structure at 43 percent debt and 57
9 percent equity as Southern Missouri Natural Gas
10 asks because that it is how Southern -- Summit
11 Natural Gas Missouri actually provided service
12 during the test period?

13 A. That is correct.

14 Q. Is it correct then to conclude that the
15 capital structure of Summit Natural Gas was used
16 in that case rather than in the parent?

17 A. That is correct.

18 Q. The report and order also indicates the
19 positions of the parties on page 36 on the cost
20 of equity issue; is that correct?

21 A. Yes, it does.

22 Q. Does the report and order indicate that
23 the Commission adopted a return on equity of
24 10.8 percent in that case?

25 A. It does.

1 Q. And that was the high end of your
2 recommended range in that case; is that right?

3 A. That is correct.

4 Q. With the exception of our current case
5 involving Laclede and MGE, have you presented
6 cost of capital testimony personally at any
7 natural gas case that's more recent than the
8 Summit Natural Gas case?

9 A. Personally, no.

10 Q. Okay.

11 JUDGE DIPPELL: Is that all you have
12 on that exhibit, Mr. Fischer?

13 MR. FISCHER: Yes.

14 JUDGE DIPPELL: I'm going to go
15 ahead and allow -- we've talked about capital
16 structure in various other cases throughout this
17 whole thing. I'm going to take official notice
18 of that report and order.

19 MR. WOODSMALL: Can I make my
20 objection first and then you can overrule it?

21 JUDGE DIPPELL: Okay. Go ahead.

22 MR. WOODSMALL: Cross-examining him
23 on it is fine, but putting it in as evidence and
24 claiming that --

25 JUDGE DIPPELL: It's not --

1 MR. WOODSMALL: -- these are facts,
2 it -- I have no problems with him assigning to
3 it, but --

4 JUDGE DIPPELL: I'm taking official
5 notice of it.

6 MR. WOODSMALL: But it's not
7 evidence?

8 JUDGE DIPPELL: It's not the law and
9 it's not a --

10 MR. THOMPSON: Mr. Fischer promised
11 he was going to show us the relevance. He has
12 not.

13 JUDGE DIPPELL: He did in fact show
14 us the relevance. We have talked about capital
15 structure, we have talked about past cases and
16 how the Commission has ruled.

17 MR. WOODSMALL: And to finish my
18 objection --

19 JUDGE DIPPELL: Finish your
20 objection, Mr. Woodsmall.

21 MR. WOODSMALL: -- I have no problem
22 stipulating to the fact that the Commission has
23 disagreed with Mr. Murray on ROE and capital
24 structure in other cases, but to then put this
25 into evidence and claim that 57 percent is

1 somehow relevant to Laclede is a reach. The
2 Company doesn't even include Summit Natural Gas
3 in their proxy group or in their peer group that
4 they measure against. Similarly, to claim that
5 giving 10.8 percent to Summit Natural Gas is
6 somehow applicable to Laclede here is also
7 completely irrelevant.

8 So I will stipulate to the fact that
9 the Commission has disagreed with Mr. Murray in
10 the past on certain things, but that is all
11 irrelevant as to what is the appropriate capital
12 structure and ROE here.

13 JUDGE DIPPELL: I still am going to
14 take official notice. I believe it is relevant,
15 though all of your arguments go toward the
16 weight and you can include those in your brief.

17 MR. FISCHER: Thank you, Judge. I
18 was merely trying to short-circuit this a little
19 bit too.

20 BY MR. FISCHER:

21 **Q. Mr. Murray, we've talked about earlier**
22 **in this case the last decision by the Missouri**
23 **Public Service Commission in a natural gas case,**
24 **which was the Liberty case. Do you recall that?**

25 A. Yes, I do.

1 MR. FISCHER: And, Judge, I'm going
2 to ask a couple of questions, but I'd like for
3 you to take official notice of that case as
4 well. That was Case No. GR-2014-0152.

5 MR. WOODSMALL: Same objections.

6 JUDGE DIPPELL: Same -- can you
7 state what --

8 MR. WOODSMALL: Just to clarify,
9 when you take official notice, does that mean it
10 is evidence or how do you mean when you take
11 official notice?

12 JUDGE DIPPELL: Under Statute
13 536.070, the Commission is allowed to take
14 official notice, and that's as far as I'm going
15 to go --

16 MR. WOODSMALL: Okay.

17 JUDGE DIPPELL: -- until a later
18 date.

19 MR. WOODSMALL: Okay.

20 BY MR. FISCHER:

21 Q. I'd like to show you a portion of that
22 on the cost of capital issue. (Tendering
23 document to witness.)

24 JUDGE DIPPELL: Mr. Fischer, can
25 you tell me that case number again?

1 MR. FISCHER: Yes, it's
2 GR-2014-0152. It was issued on December 3rd,
3 2014. And if you'd like a copy, Judge, I've got
4 one here, we can mark it, but I just was asking
5 it to be taken official notice of.

6 JUDGE DIPPELL: Proceed,
7 Mr. Fischer.

8 MR. FISCHER: Okay.

9 BY MR. FISCHER:

10 Q. If you'd turn to page 29 of that
11 decision, Mr. Murray.

12 A. (Witness complying.)

13 Q. There is a -- just a short paragraph
14 where it has the Commission's decision at the
15 top of the page. Do you see that?

16 A. (Reviewing document.)

17 I only see the ROE. I don't see the
18 capital structure.

19 Q. Well, I think -- I'm asking you to turn
20 to page 29 where it talks about -- I guess this
21 is actually the ROE.

22 A. Oh, it's just ROE?

23 Q. Yeah.

24 A. Okay. I'm sorry.

25 Q. It says there that "The Commission

1 finds this issue in favor of Liberty. The
2 Commission will set the return on equity at
3 10.0 percent, which is the bottom of the range
4 Liberty proposed. Such a return on equity is
5 commensurate with returns of other corporations
6 with corresponding risks and will ensure
7 confidence in the financial integrity of the
8 Company and is near the midpoint of the above
9 mentioned zone of reasonableness."

10 Do you see that?

11 A. I do.

12 Q. Okay. I think Mr. Hevert was a
13 witness in that case, wasn't he, for the
14 Company?

15 A. I don't recall. Sorry.

16 Q. Do you recall that Mr. Zephania
17 Marengapo [sic] was a Staff witness in that
18 case?

19 A. It's Marevangepo. And, yes, I do
20 recall.

21 Q. I apologize. Marevangepo?

22 A. Yes, sir.

23 Q. And would you have supervised him as
24 the head of the unit?

25 A. I did.

1 Q. Would you turn to page 19 of that
2 report and order to paragraph 22.

3 A. (Witness complying.)

4 Is that -- I'm just trying -- is it
5 just ROEs or capital structure?

6 Q. Well, this is on ROE.

7 A. Okay. And page -- I'm there.

8 Q. Okay. On paragraph 22, it indicates
9 that the midpoint of Mr. Marevangepo's
10 recommended return on equity range is 8.7
11 percent, which would give Liberty a return on
12 equity more than 60 basis points lower than any
13 return on equity at any state commission in at
14 least 30 years." Is that what it says?

15 A. That's what it says.

16 Q. I believe in this case you've testified
17 that the actual cost of equity for Spire
18 Missouri's operating units is presently in the
19 range of 6.9 percent to 7.7 percent; is that
20 right?

21 A. That is correct.

22 Q. Is it correct that the high end of your
23 cost of equity range of 7.7 percent is 100 basis
24 points lower than the 8.7 percent return on
25 equity that Staff recommended in the Liberty

1 case?

2 A. It is.

3 Q. And that 8.7 percent ROE, according to
4 the Commission's findings in the Liberty case,
5 was more than 60 basis points lower than any
6 return on equity at any state commission in at
7 least 30 years?

8 A. I think that was his recommendation, I
9 mean. But that's -- that's not my
10 recommendation, so it's a little different, but
11 I understand what you're -- yeah, that is
12 correct.

13 Q. But you did indicate that you had
14 supervised him and approved that recommendation
15 in that case?

16 A. Yes. It was cost of equity --
17 allowable return based on the cost of equity.

18 Q. Well, isn't the reason that you're not
19 recommending that the Commission authorize an
20 ROE in this case as low as what you believe is
21 the real cost of equity, is that the reason,
22 because it's never been adopted in 30 years?

23 A. No. The reason is I'm paying attention
24 to what the Commission has adopted in cases in
25 recent past that take into consideration all the

1 capital market activities that we have at this
2 point in time and as much as I still believe
3 that it's -- the capital markets support fairly
4 low cost of equity. I mean, we do have priced
5 earnings ratios for utilities at all time highs
6 and dividend yields at all time lows. I
7 recognize there is some hesitancy to come down
8 to actual cost of equity which is corroborated
9 by market participants that actually invest. So
10 my point being --

11 Q. You recognize, don't you, that such a
12 low range of 6.7 to 7.7 hasn't been found
13 reasonable by any state agency for many years,
14 correct?

15 A. For an allowable return, that's
16 correct.

17 Q. And if we refer to page 28 of that
18 Liberty case, in paragraph 26 it describes --
19 well, here, it says "The Commission has
20 described a 'zone of reasonableness' extending
21 from 100 basis points above to 100 basis points
22 below the recent national average of awarded
23 ROEs to help the Commission evaluate ROE
24 recommendations." Is that right?

25 A. Yes. I can actually remember when that

1 zone test was created. It was in 2004.

2 Q. Okay, good. And then it goes on to say
3 "Because the evidence shows the recent national
4 average ROE for gas utilities is 9.69 percent,
5 that zone of reasonableness for this case is
6 8.69 to 10.69," correct?

7 A. That is correct.

8 Q. And in that case the Commission found
9 an ROE of 10 percent even for -- was reasonable
10 for Liberty or in the upper part of the zone of
11 reasonableness; is that true?

12 A. As applied to their capital structure,
13 that is correct.

14 Q. On page 40 of the Staff Cost of Service
15 Report at line 14 -- do you have that?

16 A. I'm there.

17 Q. Page 40 at line 14, you state that "The
18 average allowed ROEs for gas utilities are
19 closer to 9.5 for the first six months of 2017."
20 Is that right?

21 A. I do.

22 Q. So if the Commission applies its zone
23 of reasonableness concept in this case, those
24 zone of reasonableness would be a hundred basis
25 points above and a hundred basis points below

1 that 9.5 recent national average for gas
2 utilities; is that right?

3 A. I mean, that's what -- just taking a
4 pure average without looking at the details. I
5 think we've learned a little bit more as time
6 has gone on.

7 Q. And so that would mean that the zone of
8 reasonableness would be 8.5 to 10.5 using that
9 9.5 recent -- or national average?

10 A. If that was assumed to be the
11 reasonable average, that's correct.

12 Q. So a 10.35 would be within that range
13 of reasonableness, correct?

14 A. Yes, it would.

15 Q. And, of course, if the national average
16 goes up, so would that zone of reasonableness,
17 correct?

18 A. Again, depending on what you believe
19 should be in that national average, yes.

20 Q. Well, in this case, while you
21 testified, -- and I think you just reiterated
22 that you still believe the actual cost of equity
23 for Spire is 6.9 to 7.7, you've recognized that
24 that range is below the authorized returns that
25 other state agencies are giving in recent years,

1 correct?

2 A. Can I clarify something? This is not
3 something that I just pulled out of thin air.
4 It's corroborated.

5 Q. Well, I just really need an answer.

6 A. Okay.

7 Q. Is that a yes?

8 A. Please repeat the question.

9 Q. Yeah. While you've testified that in
10 your opinion the actual cost of equity for Spire
11 is 6.9 to 7.7, you've recognized that that range
12 is below the authorized returns of any state
13 regulatory agencies in recent years?

14 A. Oh, without a doubt, yes.

15 Q. So, instead, you're recommending the
16 Commission utilize an ROE of 9.25 and your upper
17 end of that range is 9.5; is that right?

18 A. I recommended a range of nine to nine
19 and a half.

20 Q. So nine and a half would be -- nine and
21 a half would be in the high end of the range?

22 A. Yes.

23 Q. Is it correct that you're not
24 recommending an ROE based upon your professional
25 opinion of what is the actual cost of equity for

1 **Spire Missouri?**

2 A. That is correct.

3 **Q. Your actual cost of equity is simply**
4 **not appropriate in light of what other natural**
5 **gas companies are being authorized around the**
6 **country?**

7 A. As taking into consideration allowable
8 returns, that is correct.

9 **Q. As I understand your testimony on**
10 **page 10 of the Staff's Cost of Service Report,**
11 **you used the Commission's recently authorized**
12 **ROE of 9.5 percent for KCPL in Case No.**
13 **ER-2016-0285 as a benchmark to determine the**
14 **just and reasonable allowable return on equity**
15 **for Laclede and MGE in this case; is that**
16 **correct?**

17 A. Yes.

18 **Q. Now, since the Commission issued its**
19 **order in that case, is it correct that the**
20 **Federal Reserve has raised interest rates?**

21 A. The Federal Reserve has raised Fed
22 funds rate at a short-term rate. That --
23 interest rates, long-term rates are more market
24 oriented.

25 **Q. On page 11 of your Staff Cost of**

1 Service Report at line 7, you state "As recently
2 as its June 2017 meeting, the Federal Open
3 Market Committee agreed to raise the benchmark
4 rate a quarter point which stands at 1.00 to
5 1.52 percent. Since December of 2015, the Fed
6 has increased the rate four times." Is that
7 correct?

8 A. That is correct.

9 Q. Would you agree that there's been a
10 trend for the Fed to periodically raise interest
11 rates since the end of 2015?

12 A. The Fed funds rate. I think it's
13 important to specify what rates. They have
14 control over the Fed's fund rate and that has
15 been increased, but the long-term rates have not
16 followed suit.

17 Q. And the Fed has raised those rates four
18 times, correct, since 2015?

19 A. That is a fact.

20 Q. Would you agree that the interest rate
21 hike by the Federal Reserve is an indication the
22 Fed is confident about the pace of the growth in
23 the U.S. economy?

24 A. I don't believe they're confident about
25 the pace. It's a kind of wait and see and see

1 how the information comes in.

2 Q. In your job as the head of the
3 financial unit, do you follow the comments of
4 the Chair of the Federal Reserve?

5 A. Through -- through financial media,
6 yes.

7 Q. Did you see the recent news reports at
8 the end of November that the Federal Reserve
9 chair, Janet Yellen expected to continue to
10 raise interest rates gradually?

11 A. I recall that.

12 Q. Did you also see the reports that the
13 new Chair that's been nominated, Jerome Powell,
14 also intends to continue that trend?

15 A. Taking into consideration the
16 flexibility of -- as market data comes in and
17 adjusting as necessary, that's correct.

18 Q. Do you agree with Miss Ahern's comments
19 that she's expecting -- or that the market is
20 expecting the Fed rates to be -- interest rates
21 to be raised in December of this year?

22 A. The Fed funds rate, yes.

23 Q. Okay. Is it also true that since the
24 Commission issued its order in the last KCPL
25 case, the rate of annual growth of the GDP has

1 **been reported in excess of 3 percent?**

2 A. I believe it was 3 percent in each of
3 the last two quarters.

4 **Q. And that was an improvement over**
5 **previous years' growth rates, correct?**

6 A. There were 3 percent quarters in the
7 previous years as well. They weren't sustained.

8 **Q. But now they're in excess of 3 percent**
9 **today in the last quarter?**

10 A. I'm just telling you I recall there
11 were 3 percent quarter GDP rates in past years
12 since the financial crisis as well.

13 **Q. Would you agree that that's the**
14 **strongest growth that -- since the first quarter**
15 **of 2015?**

16 A. I'm not sure how much stronger, but I
17 have no reason to dispute that.

18 **Q. Okay. As I understand your testimony,**
19 **Mr. Murray, you're indicating that, while you**
20 **believe the cost of equity is less than the**
21 **average allowed ROEs around the country, you**
22 **have essentially put aside that cost of equity**
23 **analysis and instead attempted to quantify the**
24 **difference in the cost of equity of a vertically**
25 **integrated electric utility and local**

1 **distribution natural gas company; is that right?**

2 A. Yes, I'm looking at the relative
3 difference in the cost of equity between the two
4 industries, yes.

5 **Q. And you just apply that differential**
6 **between the natural gas companies and the**
7 **vertically integrated electric companies to**
8 **lower the ROE that the Commission authorized in**
9 **the KCPL case, correct?**

10 A. I'm sorry. Repeat that question,
11 please.

12 **Q. You adjusted or you applied that**
13 **differential between electric and gas risks, as**
14 **I understand your testimony, and applied that to**
15 **lower the authorized return that was granted in**
16 **the KCPL case in 2015?**

17 A. The -- I -- the lower allowed ROE I
18 recommend to the Commission. I mean, I'm not
19 lowering the authorized ROE. I'm just making a
20 recommendation.

21 **Q. Oh, I understand it's the Commission**
22 **job to do that.**

23 A. Okay.

24 **Q. But you're recommending, aren't you,**
25 **that you look at the KCPL ROE and adjust that**

1 downward because of this risk differential that
2 you believe exists; is that right?

3 A. That is correct.

4 Q. On page 28 of the Staff Cost of Service
5 Report, you also indicate that "I used a CAPM
6 analysis and survey of other indicators as a
7 check on the reasonableness of my
8 recommendation." Is that right?

9 A. I'm sorry. What page?

10 Q. It's page 28.

11 A. (Reviewing document.)

12 That's 30 to 31?

13 Q. Yeah, probably so. I didn't have a
14 line reference, but...

15 A. That is correct.

16 Q. Okay. So is it correct that you did
17 not use a CAPM analysis as the primary basis for
18 your ROE recommendation?

19 A. No, I think that corroborated my
20 7 percent cost of equity estimate, along with
21 other data.

22 Q. And then on page 43 you talk about the
23 rule of thumb method; is that correct?

24 A. Yes, that's my test of reasonableness
25 method.

1 Q. Is it correct that you did not include
2 the rule of thumb method as the primary basis
3 for your ROE recommendation?

4 A. Yes.

5 Q. And did you include anywhere in your
6 Staff Cost of Service Report or any of your
7 testimony any decision by the Commission that's
8 relied on that rule of thumb method?

9 A. It's not a primary driver. The
10 recommendation is just to test reasonableness.
11 So I don't know why that it would be, but, no, I
12 did not.

13 Q. Okay. Let's turn to the capital
14 structure issues. Did you happen to look at the
15 True-Up testimony of Laclede's witness Glenn
16 Buck where he laid out the capital structure as
17 of the true-up?

18 A. I did.

19 Q. And would it be correct that that
20 capital structure was 54.2 percent common equity
21 and 45.8 percent long-term debt?

22 A. That's his recommended capital
23 structure. I don't agree that that's the actual
24 cap structure, but yes.

25 Q. Okay. On page 21 of the Staff Cost of

1 Service Report at line 18 --

2 A. Yes.

3 Q. -- you say there at line 18 "Based on
4 my analysis, I recommend that the capital --
5 that the Commission use Spire Inc.'s capital
6 structure with an average level of short-term
7 debt in setting the authorized ROR" -- which is
8 return on rate of return; is that right?

9 A. Yes.

10 Q. -- "for Laclede and MGE." Is that
11 correct?

12 A. Yes.

13 Q. And then you go on to explain that
14 Spire Inc.'s consolidated capital structure
15 contained 46.05 percent common equity with
16 short-term debt included and 51.3 percent common
17 equity with short-term debt excluded; is that
18 right?

19 A. That is correct.

20 Q. Is it correct that the last time the
21 Staff reviewed the capital structure issue for
22 Laclede and MGE was in Case No. GR-2014-0007,
23 which was the rate case involving MGE after it
24 had been acquired by Laclede?

25 A. In a rate case, that's correct.

1 MR. FISCHER: Your Honor, I would
2 like to have an exhibit marked.

3 JUDGE DIPPELL: I'm going to mark
4 your previous report and order as Exhibit 59, so
5 we're up to 60.

6 MR. FISCHER: Okay.

7 (SPIRE EXHIBIT NO. 59 AND 60 MARKED
8 FOR IDENTIFICATION.)

9 BY MR. FISCHER:

10 Q. Mr. Murray, does this appear to be one
11 of the Staff's accounting schedules that
12 appeared in Case No. GR-2014-0007?

13 A. It is.

14 Q. And does this appear to be the capital
15 structure schedule for the true-up period ending
16 December 31st, 2013 which was included in those
17 schedules in the MGE's last rate case?

18 A. It is.

19 Q. Is it correct that this schedule shows
20 that the Staff's capital structure for the
21 true-up in that case contained a 53.56 percent
22 common equity ratio and a 46.44 percent
23 long-term debt ratio?

24 A. And no short-term debt, that's correct.

25 Q. And no short-term debt. That was my

1 next question.

2 So is it correct that the Staff's
3 recommended use of a 53.56 equity ratio with no
4 short-term debt, that's what your recommendation
5 was in that case?

6 A. Yes, it was.

7 Q. In this case Spire Missouri's
8 recommending an equity ratio of 54.2 percent
9 with no short-term debt included; is that your
10 understanding?

11 A. That is correct.

12 Q. So in the last MGE case, Staff
13 recommended a 53.56 equity ratio in the true-up
14 and Spire Missouri in this case is recommending
15 a 54.2 percent without short-term debt, correct?

16 A. There are different circumstances in
17 this case, but that is correct.

18 Q. Would it be correct to conclude that
19 the equity ratio used by Staff in MGE's last
20 rate case is less than one percentage point
21 lower than what Spire Missouri's recommending in
22 this case?

23 A. That is correct.

24 Q. To be more precise, Spire Missouri's
25 actual capital structure as of the true-up date

1 is only 0.64 percent higher than what Staff was
2 using in the MGE last rate case?

3 A. That is correct.

4 Q. I would like to try to be clear in the
5 transcript for the next couple of questions. So
6 if it would be okay with you, Mr. Murray, I
7 would like to describe Spire Missouri's capital
8 structure as Laclede's capital structure and
9 refer to the parent Spire Inc.'s capital
10 structure as just the consolidated capital
11 structure of the parent. Would that be all
12 right?

13 A. I understand.

14 Q. Okay. Staff agrees that Laclede's
15 capital structure includes the first mortgage
16 bonds issued to outside investors by the
17 operating company Laclede, correct?

18 A. Yes.

19 Q. And, in other words, Laclede, they
20 issued their own -- it issues its own long-term
21 debt, correct?

22 A. Yes.

23 Q. Laclede issues bonds to the market that
24 support its regulated operations, correct?

25 A. Yes.

1 Q. Laclede's long-term debt is secured by
2 the operating company's own assets and not the
3 assets of the parent company, correct?

4 A. Yes.

5 Q. And Laclede's long-term debt is not
6 secured by the assets of the parent's other
7 public utilities, Alabama Gas Corporation or the
8 subsidiaries of Energy South, correct?

9 A. Yes.

10 Q. And Laclede's assets do not guaranty
11 Alagasco's long-term debt; is that correct?

12 A. Yes.

13 Q. And Laclede's assets do not guaranty
14 the long-term debt for other subsidiaries of
15 Energy South, former Energy South subsidiaries?

16 A. Yes.

17 Q. And Laclede's assets do not guaranty
18 the long-term debt of Spire Marketing; is that
19 right?

20 A. I don't think Spire Marketing has
21 long-term debt, but...

22 Q. Okay. And Laclede's assets do not
23 guaranty the operations of Spire Marketing,
24 correct?

25 A. Yes.

1 Q. And Laclede's assets do not guaranty
2 the operations of Spire STL Pipeline; is that
3 your understanding?

4 A. Yes.

5 Q. And the Staff agrees that the Missouri
6 Public Service Commission has approved the
7 long-term debt issuances of Laclede, the
8 operating utility in Missouri, correct?

9 A. Yes.

10 Q. Has the Missouri PFC, approved any
11 long-term debt issuance for Alagasco?

12 A. No.

13 Q. Has the Missouri Commission approved
14 any long-term debt issuances for any other Spire
15 public utilities operating outside of the state
16 of Missouri?

17 A. No.

18 Q. Does Staff agree that Laclede does not
19 obtain any long-term debt from its parent Spire
20 Inc.?

21 A. Please re- -- ask that question again,
22 please.

23 Q. Do you agree that the Laclede, the
24 public utility, does not receive debt from Spire
25 Inc., the parent?

1 A. I do not.

2 Q. You don't agree with that?

3 A. I do not agree with that.

4 Q. Okay. Do you agree that Laclede's
5 long-term debt is secured by its own public
6 utility assets and not the assets of the parent?

7 MR. THOMPSON: Asked and answered.

8 MR. FISCHER: If we got it, could --
9 I can withdraw it if he has answered that.

10 MR. THOMPSON: He has answered that.

11 JUDGE DIPPELL: Was that --

12 Mr. Thompson, are you saying that was the last
13 question?

14 MR. THOMPSON: No, I'm saying it was
15 one of the previous questions.

16 JUDGE DIPPELL: Okay. I'm going to
17 let him answer it again just because it's going
18 to take too much time to go back through the
19 transcript.

20 MR. THOMPSON: Very well.

21 THE WITNESS: Please repeat the
22 question.

23 BY MR. FISCHER:

24 Q. Oh, sure. Do you agree that Laclede's
25 long-term debt is secured by its own public

1 utility assets and not the assets of the parent?

2 A. Yes.

3 Q. On a previous question you disagreed
4 that -- I think that we didn't -- that the
5 Laclede Gas Company didn't have debt from the
6 parent, our -- would you explain why that is?
7 Is that because of the commercial paper?

8 A. No. There's been proceeds and when
9 Laclede -- Laclede Group has issued long-term
10 debt specifically before the transactions, but
11 where they would issue long-term debt and they
12 admitted themselves that they don't need any
13 capital proceeds for their LER operations and
14 there would be cash infusions into -- into
15 Laclede Gas Company. So, you know, if you
16 follow their cash flow, there's only -- and
17 there's investments into the Laclede Gas
18 subsidiary, there's really no other way to
19 explain it than the proceeds from the debt
20 issued at Laclede Group were infused into
21 Laclede Gas. So that's why I disagree with
22 that.

23 Q. And it's infused as equity, correct?

24 A. It may be infused as equity. You have
25 a lot of things going on, there's a lot of

1 moving parts. There's, you know, short-term
2 loans made from Laclede Group to Laclede Gas
3 even before the commercial paper. But now with
4 the commercial paper -- consolidated commercial
5 paper program as of January 2017, yes, Spire
6 Incorporated consolidated directly borrows from
7 the commercial paper markets and loans those
8 proceeds to its subsidiaries.

9 **Q. You agree that the long-term debt of**
10 **Laclede, the public utility, is used to support**
11 **the public utility operations of Laclede,**
12 **correct?**

13 A. Yes.

14 **Q. Do you agree that the parent's capital**
15 **structure includes long-term debt and common**
16 **equity of Alagasco?**

17 A. Yes.

18 **Q. Do you agree that the parent's capital**
19 **structure includes the common equity capital of**
20 **the subsidiaries that were formerly with Energy**
21 **South?**

22 A. Yes.

23 **Q. The capital structure of the parent**
24 **also supports unregulated activities of Spire**
25 **Marketing, an unregulated subsidiary of the**

1 **parent; is that right?**

2 A. Yes.

3 **Q. And does the parent have any other**
4 **unregulated activities that you're aware of?**

5 A. They have several subsidiaries. I
6 don't know if it's very material at this point
7 in time, but I think you've covered the material
8 entities.

9 **Q. Okay. And the capital structure of the**
10 **parent also supports the activities of Spire STL**
11 **Pipeline; is that right?**

12 A. Yes.

13 **Q. Now, that's an interstate pipeline; is**
14 **that your understanding?**

15 A. At least FERC regulates, yes, so it
16 would be interstate.

17 **Q. Yes, it's under the jurisdiction of the**
18 **FERC?**

19 A. Yes.

20 **Q. The operations of this interstate**
21 **pipeline company would also be supported by the**
22 **parent's capital structure, correct?**

23 A. Yes, I don't think they've set up
24 separate facilities at this point.

25 **Q. Do you believe that an interstate**

1 pipeline has somewhat different risk profiles
2 than a regulated local distribution company like
3 Laclede?

4 A. I think they're both viewed fairly as
5 low risk operations. I can't say that, you
6 know, there's a lot of differentiation within
7 the investment community for pipelines versus
8 LDCs.

9 Q. Are the FERC-authorized ROEs for
10 interstate pipelines typically higher than what
11 you're recommending for Laclede in this case?

12 A. Yes.

13 Q. Does Laclede, the operating utility,
14 have access to any capital that is being used by
15 Alagasco or the subsidiaries of Energy South?

16 MR. THOMPSON: I'm going to object.
17 There's been no showing that Mr. Murray would
18 know that.

19 MR. FISCHER: If he doesn't know, he
20 can say that, Judge.

21 JUDGE DIPPELL: I'll let him answer.

22 THE WITNESS: Well, and this -- I
23 mean, there's a lot of indirect influences. I
24 know that there was, you know, discussion
25 earlier about cash being fungible and,

1 obviously, there's dividend that come up from
2 subsidiaries and loans that go back down to the
3 subsidiaries and, you know, to the extent that
4 long-term debt is issued at Alagasco and to the
5 Treasury and there's a dividend paid to Spire
6 Incorporated and then some of those proceeds
7 were from the long-term debt issuance, just like
8 in the past where Laclede Group would issue
9 long-term debt and make either equity infusions
10 or small -- or short-term loans to the
11 subsidiary, there's a lot of fungibility. So I
12 agree that this is where the debt is issued, but
13 I don't agree that everything has been kept
14 separate.

15 BY MR. FISCHER:

16 **Q. Well, do you know that Laclede has**
17 **access to capital from Alagasco?**

18 A. Indirectly through Spire. If there's,
19 you know, loans being made to Spire Missouri for
20 commercial paper and through dividends through
21 Alagasco, it -- they -- they allocate the
22 capital where it's needed.

23 **Q. Were you involved in the Laclede**
24 **holding company stipulation?**

25 A. I was.

1 Q. Were you --

2 A. No. You're talking 2001.

3 Q. Yeah.

4 A. I mean, I've been around for awhile,
5 but I was not directly involved in that.

6 Q. Okay, I'll let that go.

7 Do you happen to have Mr. Buck's
8 True-Up testimony?

9 A. I do.

10 Q. Would you look at his testimony where
11 he lays out the long-term debt and equity and it
12 aggregates to a little more than \$2.1 billion.
13 Is that right, on page 2?

14 A. What page? Can you help me, please?

15 Q. Page 2. He's got four pieces, but it's
16 the true-up, correct?

17 A. (Reviewing document.)

18 I see that.

19 Q. Okay. Now, according to -- did you
20 review Miss Ahern's rebuttal testimony?

21 A. I did.

22 Q. Let's short-circuit it a little bit.
23 On page 6 of her testimony, she laid out the
24 parent's consolidated capital as of December 31,
25 2016 and indicated it was about 3.6 billion.

1 Do you have any dis- -- do you have any
2 reason to disagree with that?

3 A. (Reviewing document.)

4 Q. If you're looking it up, it's page 6,
5 line 24.

6 MR. THOMPSON: Is that the direct?

7 MR. FISCHER: Rebuttal.

8 MR. THOMPSON: Thank you.

9 THE WITNESS: (Reviewing document.)

10 It's right from their 10-K, so I have
11 no reason to dispute that.

12 BY MR. FISCHER:

13 Q. Okay. So is it correct that the total
14 capital long-term debt and equity for Laclede is
15 about one and a half billion dollars less than
16 total capital of the parent Spire Inc.

17 A. Yes.

18 Q. And that's what you would expect, isn't
19 it, because the parent's operations include more
20 than the regulated activities of Laclede or
21 Spire Missouri, correct?

22 A. Yes.

23 Q. I believe you indicated earlier that
24 the Commission approved an equity ratio of
25 57 percent equity in the Summit Natural Gas

1 case; is that right?

2 A. Yes.

3 Q. I believe you also indicated Laclede is
4 proposing an equity ratio of 54.2 percent in
5 this case --

6 A. Yes.

7 Q. -- correct?

8 A. Yes.

9 Q. That 54.2 percent equity ratio that
10 Laclede is proposing in this case is less than
11 the 57 percent equity ratio approved by the
12 Commission in the Summit Natural Gas case; is
13 that right?

14 A. That's a fact. That's correct.

15 Q. Let's talk about short-term debt for a
16 second. Is Staff proposing to include
17 short-term debt in the Company's capital
18 structure for rate-making purposes?

19 A. Yes.

20 Q. Isn't it true that the Commission did
21 not include short-term debt in the capital
22 structure of -- for Summit Natural Gas -- I
23 think we've already addressed that -- in 2014?

24 A. Yes, that's true.

25 Q. And short-term debt was not included in

1 the Liberty case we talked about either,
2 correct?

3 A. That is correct.

4 Q. You also discussed the 2014 KCPL rate
5 case in your Staff report. Isn't it correct
6 that the Commission did not include short-term
7 debt in the capital structure in that case?

8 A. That's a fact.

9 Q. Are you aware of any KCPL or GMO cases
10 in which the Commission has included short-term
11 debt in the capital structure used for
12 rate-making since you've been employed here?

13 A. Well, being that they had quite bit of
14 construction and the construction work in
15 progress exceeded short-term debt, I don't
16 believe there was.

17 Q. In the last Ameren Missouri case isn't
18 it true that the capital structure used for
19 rate-making did not include short-term debt?

20 A. Again, for the same reason.

21 Q. Did you cite any case in your Staff
22 Cost of Service Report where Ameren Missouri had
23 any short-term debt included in the capital
24 structure for rate-making?

25 A. I did not -- if there was, it's been

1 some time ago.

2 MR. FISCHER: Thank you for your
3 indulgence. That's all the questions I have.
4 Thank you.

5 JUDGE DIPPELL: Thank you,
6 Mr. Murray. You may step down.

7 MR. THOMPSON: Redirect.

8 JUDGE DIPPELL: Oh, I'm sorry. Oh,
9 I was done.

10 Are there questions from the
11 Commissioners.

12 CHAIRMAN HALL: (Nodding.)

13 JUDGE DIPPELL: Chairman Hall.

14 QUESTIONS BY CHAIRMAN HALL:

15 Q. Good afternoon.

16 A. Good afternoon, Chairman.

17 Q. Is it fair to say that sometimes Staff
18 recommends, sometimes the Commission adopts a
19 subsidiary-specific capital structure, sometimes
20 Staff recommends, sometimes the Commission
21 adopts a consolidated capital structure?

22 A. Yes. And, actually, Staff has
23 recommended hypotheticals and the Commission
24 still recommended a consolidated capital
25 structure. So, you know, we don't -- you listen

1 to the evidence, and I understand that.

2 **Q. Are there some broad principles that**
3 **you would recommend the Commission employ to**
4 **make that decision subsidiary specific versus**
5 **consolidated?**

6 A. Well, obviously, I mean, I know it's,
7 you know, a situation that we're all well aware
8 of where there's a holding company that does not
9 issue debt at the holding company level to
10 leverage its transactions that does not place
11 financial risk on its subsidiaries. I mean,
12 that's definitely a significant concern to Staff
13 because to the extent that the holding company
14 issues significant amounts of debt at its level,
15 it constrains the credit rating of the
16 subsidiary, and to the extent that the
17 subsidiary is going to, you know, have a higher
18 ratio and the ratepayers are going to provide
19 more cash flow -- I mean, I understand from a
20 business model perspective as to why they would
21 want to continue to have a higher equity ratio
22 at the subsidiary, because that supports the
23 debt that they have at the holding company. So
24 the more that -- you know, the more that, you
25 know, they push that and, obviously, that makes

1 a big difference on the revenue requirement,
2 then the more financial risk they can take at
3 the holding company level, which definitely
4 impacts the credit rating at the subsidiary
5 level, you know, more so with S&P, you know, but
6 also to quite a bit of extent with Moody's. So
7 it affects their credit rating.

8 **Q. But is that the only principle that you**
9 **think the Commission should employ in making**
10 **this decision or are there some other**
11 **considerations?**

12 A. It's the debt capacity of these low
13 risk gas operations. These are low risk gas
14 utility operations, and in my opinion the
15 holding company, you know, they understand that
16 and they understand that's how they can create
17 value with these transactions.

18 I don't have a problem with, obviously,
19 creating value with transactions, but to the
20 extent that you have to start taking into
21 consideration all the holding company debt as to
22 how you manage your subsidiary debt
23 considerations, even to the extent you use a --
24 you could use a shorter term tenor at the
25 holding company because of the fact that you

1 typically don't want to, you know, have a
2 30-year debt at the holding company. So that
3 influences the subsidiaries' financial
4 management to the point where they, you know,
5 will be more likely to issue longer-tenored debt
6 because it's -- it is at the subsidiary, it is
7 right at the assets, but as a -- I mean,
8 regardless, if it's the same risk profile, a
9 30-year debt is going to be more costly than a
10 10-year debt.

11 So there's just no way to unwind this
12 to show -- you know, to ensure that there's
13 going to be, you know, a management of the
14 subsidiary capital structure in the best
15 interest of the ratepayers that provide these
16 low risk cash flows. At the FFO-to-debt that
17 Spire Incorporated consolidated, you know, it
18 has right now is about 16 percent. The
19 FFO-to-debt for Spire Missouri is 21, 22
20 percent. That should, you know, allow for a
21 higher credit rating. But when you have a
22 holding company that has over a billion dollars
23 of debt that it's issued for its acquisitions,
24 that has an effect on the credit quality of the
25 subsidiary, and therefore, even though the

1 subsidiary has a higher equity ratio -- and, you
2 know, in the past when Laclede Group had similar
3 or actually even higher -- you know, it had a
4 higher equity ratio on a consolidated basis
5 before it start making these acquisitions. That
6 supported the credit quality of the subsidiary,
7 and therefore, the ratepayers got credit for --
8 when I say "credit," a more financially sound
9 flexible entity.

10 The holding company leverage, it puts
11 financial risk, and that's what has changed
12 since 2013/14 is we have much more aggressive
13 financial policy at the holding company level
14 than we did before.

15 **Q. Okay, I understand that, I appreciate**
16 **that and, I agree that that is an important**
17 **criteria.**

18 **What about other aspects, though? I**
19 **mean, if you have a truly independent subsidiary**
20 **with different board of directors, different**
21 **officers, is that something we should take into**
22 **account?**

23 **A. I'll point to, I believe, you know,**
24 **what some of the other states had done say, for**
25 **instance, New York. Each time they look at a**

1 subsidiary that asks for subsidiary capital
2 structure, they'll look at the holding company
3 and they'll look as to, you know, are there
4 sufficient ringfencing mechanisms in place.

5 And ringfencing is used way too
6 loosely. Ringfencing is a very structural legal
7 protection. It's not just, you know, a few
8 conditions that they commit to with the
9 regulator that may or may not be enforced. It
10 is -- such as an independent director.

11 Actually, S&P has more stringent
12 criteria as to what is considered an independent
13 director than the New York Stock Exchange
14 does -- excuse me -- the SEC does. And so, you
15 know, whether or not you need a bankruptcy
16 remote entity or a separate management,
17 obviously, they -- you know, Spire is embracing
18 the consolidated type of management where they
19 use the one brand name. I mean --

20 **Q. So does Spire Inc. and Spire Missouri**
21 **have the same directors?**

22 A. They have the same -- yeah, the board
23 of directors is the same. There might be one
24 separate -- one different person, but for the
25 most part, their officers and the directors are

1 mirrors.

2 **Q. Is that something we should take into**
3 **account in making this determination?**

4 A. This is getting -- there's a lot of
5 legal issues and I don't -- I don't want to, you
6 know, pretend like I have not looked at these
7 issues, but I do know when we explored this with
8 other companies, they've told us that they need
9 outside counsel to look at this closer. So I
10 don't want to be -- you know, to give you the
11 impression that I have all the answers as to how
12 this can be completed. But, yes, those are
13 things that would need to be looked at to
14 determine whether you're going to get more
15 rating separation.

16 **Q. Any other criteria, any other**
17 **principles, any other --**

18 A. Separate credit facilities. I mean,
19 like I've said, they've actually gone to
20 consolidated credit facility, but...

21 I say credit facility. Commercial
22 paper. They do have -- the credit facility that
23 backs the commercial paper still has separate
24 sub-limits for the credit- -- different
25 entities, but Spire is actually going to the

1 commercial paper markets and lending into it.

2 But, yeah, just as far as the
3 intercompany transactions, to the extent that,
4 you know, there is any -- you know, I guess
5 right now we have, you know, in mid lease, so we
6 have -- and we've done this in some of our
7 stipulation agreements that if they fall below
8 investment grade, then there's going to be
9 restriction, but that's fairly reactionary. And
10 so, yes, if you had more legal structural as far
11 as somebody looking out for the interest of the
12 individual operating entity, that would be, you
13 know, more proactive.

14 **Q. How does -- how do the credit rating**
15 **agencies deal with Spire Inc. versus Spire**
16 **Missouri? Do they do separate ratings for both?**

17 A. At S&P, they approach it differently
18 and that's -- actually, it ties in with some of
19 the different viewpoints of the witnesses. But
20 Spire -- excuse me -- S&P generally if they
21 don't -- I mean, and they're much more stringent
22 as to what they consider to be true separation.
23 It's not reactionary it's proaction --
24 proactive. So if that -- you know, if they
25 don't deem it sufficient, they're going to rate

1 all the entities based on the consolidated
2 family group of companies, which right now is A-
3 for Spire Missouri and A- for Spire Incorporated
4 consolidated.

5 **Q. So S&P does not think there is**
6 **sufficient separation to do two different credit**
7 **ratings? It does one credit rating for both?**

8 A. It does one corporate credit rating. I
9 do want to explain that Spire Missouri -- I
10 mean, this is another, I mean, thing that I'm
11 not sure exactly how -- you know, if there is
12 some benefit to this, but Spire Missouri has
13 first mortgage bonds. Spire Alabama issues
14 unsecured debt. So they do things differently.
15 So as a result, because they are first mortgage
16 bonds, they have -- they have an A rating. They
17 could have one notch better if it wasn't for the
18 affiliation with -- you know, with Spire
19 consolidated and through the greater financial
20 risk at the Spire consolidated level.

21 With Moody's, there's a -- generally a
22 constraint of three notches between the holding
23 company and a subsidiary. And Moody's has a
24 grid indicator rating of unsecured rating for
25 Spire Missouri of A, but they ultimately assign

1 it at A-. There is not a lot of information in
2 the report that explains why they do that, but
3 they are very -- you know, very upfront about
4 the 40 percent or so of debt at the consolidated
5 level as compared to -- at the holding company
6 level compared to the total debt is a concern
7 because that puts pressure on the subsidiaries.
8 It's just a natural concern of theirs, so that
9 suppresses the credit rating.

10 **Q. There's been some discussion about**
11 **whether or not using a consolidated capital**
12 **structure in this case is a deviation from prior**
13 **decisions with regards to Laclede or whether**
14 **it's a continuation of prior decisions.**

15 **And it's really kind of a hybrid**
16 **because in the past -- and this is a question.**
17 **In the past we used Laclede Group's consolidated**
18 **capital structure and now the request from -- by**
19 **Staff and some of the other parties is to use**
20 **Spire Inc. consolidated capital structure. So**
21 **there's some similarities and some differences;**
22 **is that correct?**

23 A. But Spire Inc. is just the new Laclede
24 Group. So I --

25 **Q. But it includes some entities that were**

1 **not part of the Laclede Group?**

2 A. Well, that was true -- because they --
3 I don't know when they changed their name, but
4 Laclede Group acquired Alagasco and they were
5 still Laclede Group. I don't know when they
6 changed their name.

7 But, yeah, the bottom line is the
8 difference now is the holding company -- and
9 let's just call it "the holding company"
10 regardless of the name -- has Alagasco and the
11 Energy South subsidiaries. That's what's
12 different between now and 2013 or 2014.

13 But you're correct, Laclede Group,
14 their main operation at the time besides Laclede
15 Gas was their energy marketing operations and
16 they did not -- I mean, through admission of
17 their own testimony, they did not need to issue
18 any long-term capital for Spire Marketing, but
19 they still issued long-term capital at Laclede
20 Group. So by that admission, and obviously they
21 were issuing debt at the holding company to fund
22 operations at the subsidiary.

23 Now, I think they'll say that they're
24 committing to keeping these things separate
25 going forward, but I don't know that we have

1 anything that's going to prevent that from
2 happening.

3 **Q. Okay. Let me switch gears for a**
4 **second. This chart -- I don't know the exhibit**
5 **number.**

6 JUDGE DIPPELL: I believe that was
7 56.

8 CHAIRMAN HALL: 56?

9 JUDGE DIPPELL: No, I'm sorry, 57.

10 BY CHAIRMAN HALL:

11 **Q. Have you ever seen this before?**

12 A. I've not seen this chart.

13 **Q. Were you in the hearing room when that**
14 **was discussed?**

15 A. I was.

16 **Q. So you understand roughly what it says?**

17 A. Well, I understand this is a
18 price-weighted index. This does not factor in
19 dividends, which is a critical piece with
20 utilities.

21 **Q. Well... okay.**

22 A. But so my point being is S&P 500, your
23 dividend return is not going to be nearly as
24 high as your dividend return with your
25 utilities. So it makes a big difference. This

1 is just price performance.

2 Q. Um-hum. Well, what I'm wondering is
3 I'm looking at the LDCs being significantly
4 higher performing companies to the S&P 500, and
5 I'm wondering what -- and maybe you just
6 answered this, but what I should take from that?

7 Because, I mean, I -- one thing you
8 could take from that -- and I'm not there yet,
9 so I will contemplate it -- is perhaps that is
10 simply showing that state commissions around the
11 country are awarding ROEs too high to LDCs
12 because why should they be recovering -- why
13 should their price be going up so much more than
14 the S&P 500? So if you could respond to that?

15 A. I think it is -- I mean, regardless of
16 the Fed -- I understand the Fed trying to
17 increase the Fed fund's rate, but bottom line
18 is -- and you guys just evaluated this back in
19 2016. In 2016, you know, we were at all time
20 lows for interest rates in the middle of 2016.
21 Obviously, at the end of 2016, you had, you
22 know, the Trumpflation where rates increased for
23 a short period of time from 2 point, say, 2 or
24 somewhere -- and this is a 10-year treasury --
25 to about 2.6. Utility bond yield didn't follow

1 suit, but they did increase.

2 And so point being is, even with a lot
3 of the discussion about economic growth and the
4 prospects of economic growth, utilities have
5 still -- I mean, they're trading at all time
6 highs. So the price of earnings ratio for gas
7 utilities are 25, you know, electric's 24. I
8 mean, that is incredible.

9 **Q. So does that mean that ROEs are being**
10 **set too high across the board?**

11 A. That means the cost of equity's come
12 down and we're maintaining our allowed ROEs.
13 And so, yes, the value of that cash flow that
14 comes from utilities based on our current rates,
15 with that lower discount rate, it just -- you
16 know, it -- obviously, you are going to have a
17 lower discount rate assigned to those future
18 cash flows and so you're willing to pay more
19 because you have a lower discount rate
20 because -- that makes your present value of your
21 future cash flows worth more as of today.

22 And we're kind of in -- we have been in
23 a sustained level of a long-term low -- lower
24 long-term rates, and that bears itself out in
25 utility bond yields as well as treasuries at

1 this point in time.

2 Q. Okay. Let me switch gears again.

3 My understanding of your Staff position
4 that you have articulated is that what the
5 Commission should do is look at its decision in
6 the Ameren and KCP&L rate case where we awarded
7 I think one was 9.5 and one was 9.53 and look at
8 what has happened since then and look at
9 differences between Spire and those two
10 vertically integrated electric utilities and
11 make a downward adjustment accordingly. Is
12 that, in essence, what you're suggesting?

13 A. That is correct. I am trying to be
14 useful to the Commission and allow you to look
15 at what you did in KCPL and decide whether or
16 not you think a gas asset should be any
17 different as far as allowed return.

18 Q. Okay. Well, that was characterized
19 by -- and I can't remember the witness now, but
20 a witness, a Spire witness as "looking in the
21 rearview mirror as opposed to looking forward."
22 And I was wondering if you could respond to that
23 critique?

24 A. If anything -- and this -- I'm
25 benchmarking off the nine and a half that you

1 allowed for KCPL at -- and based on information
2 at the end of 2016/early 2017 that showed, you
3 know, interest rates and dividend yields coming
4 back up a little bit for utilities.

5 As of right now, if you were looking
6 at -- I'll first focus on electric utilities and
7 go to gas, but electric utilities are trading at
8 dividend yields below 3 percent. I've never
9 seen that and it's been going on for the last
10 three months or so. And natural gas utilities
11 are -- have dividend yield of 2 and a half
12 percent.

13 So when you have the utility industry,
14 there's not a lot of big fundamental changes
15 going on that are all of a sudden going to cause
16 growth just go crazy. So it's a reaction to the
17 macro factors. And so whenever I look at the
18 investment market commentary -- so this is -- I
19 mean, I -- we do our own analysis by looking at
20 the bond yields, looking at price-earnings
21 ratios, what have you, but I also spend a lot of
22 time looking at the utility equity analysts.
23 And the utility equity analysts -- and I have --
24 there's a quote in my testimony that they use a
25 discount, a cost of equity that's 25 basis lower

1 to determine the value of gas utility stocks
2 versus electric utility stocks. They indicate
3 they use a cost of equity that's 50 basis points
4 lower to determine the value of water utility
5 cash flows versus electric utility cash flows.

6 So the point being is that there's no
7 doubt on the equity side that there's that --
8 there's that perspective and as well on the
9 credit side because, on the credit side, both
10 Moody's and Standard & Poors indicate that gas
11 utility assets have a greater ability to -- they
12 have more debt capacity than electric because
13 they use a low -- what they call "a low
14 volatility table" for gas utility companies as
15 compared to a medial volatility table for the
16 vertically integrated electric utility
17 companies. What that means is that they can
18 issue more debt and still have the same credit
19 rating as an electric if it had less debt
20 because it has lower business risk.

21 And so it's a credit and equity view
22 that gas utilities -- and also, obviously, the
23 higher credit ratings.

24 **Q. So would you respond to that critique**
25 **by saying that it's not rearview mirror analysis**

1 because it's simply benchmarking based on prior
2 decisions of the Commission and then you are
3 looking at changes since the date of those
4 orders and you are taking that into account in
5 this analysis?

6 A. Oh, yes. And that's -- actually, I
7 provide -- there's been a lot of discussion
8 about return information for gas, electric and
9 -- within this chart (indicating to document).

10 I mean, I provide that on page 14 of my
11 Staff Cost of Service Report where I provide
12 capital market performance for utilities since
13 January 1st of 2014, and the reason why I picked
14 that because that's when -- that's the general
15 period of time when you had the nine and a half
16 allowed ROEs for UE and KCPL, obviously, the
17 Liberty utilities with ten and I show that the
18 gas utility proxy group had a total return of --
19 this is my gas proxy group -- of 103 percent for
20 a compound annual return of 24.2, so 20 percent
21 per year. The electric utility proxy group had
22 a total return of 96.64 percent for a compound
23 annual return -- excuse me, of 20 -- that was
24 20.42. The gas was 21.45 percent, where the
25 S&P 500 had a compound total return of

1 43.96 percent for that same period.

2 Utilities have outperformed the markets
3 for the last five years since January 1st, 2014,
4 and specifically since the middle of 2015.

5 **Q. And why do you think utilities have**
6 **outperformed the market generally?**

7 A. It's a low yield environment. I mean,
8 we are staying in a low yield environment.

9 As somebody pointed out, the Goldman
10 Sachs, you know, indicated that anytime 10-year
11 treasuries are within the two to three percent
12 level, these low growth utility stocks will
13 trade at premium to the higher growth market.
14 And that's a flip. I mean, that's not -- I
15 don't think that's a good thing because that
16 means that -- you know, that the companies that
17 don't have as much growth prospects are trading
18 at higher premiums and, you know, I just -- it's
19 obviously an opportunity cost that -- there's
20 no -- there's no good return in bonds.

21 CHAIRMAN HALL: I think that's all I
22 have. Thank you.

23 THE WITNESS: Thank you.

24 JUDGE DIPPELL: Thank you.

25 Are there other Commissioner questions?

1 COMMISSIONER KENNEY: No.

2 COMMISSIONER RUPP: No.

3 JUDGE DIPPELL: All right. Is there
4 further Cross-Examination based on the
5 Commissioner questions from Public Counsel?

6 MR. SMITH: No questions. Thank
7 you.

8 JUDGE DIPPELL: MIEC?

9 MR. MILLS: Just briefly.

10 RECROSS-EXAMINATION BY MR. MILLS:

11 Q. With respect to Exhibit 57, you pointed
12 out that one of the salient differences between
13 Spire's performance and the S&P performance is
14 the question of dividends, correct?

15 A. Yes.

16 Q. And do you know if the dividends
17 between -- dividend policies between Spire and
18 the -- what's labeled as a peer group on this
19 exhibit are the same?

20 A. I mean, I'll just tell you that on
21 average dividend -- or utilities paid out about
22 60 percent, and I think it's just going to vary
23 a little bit between the different companies,
24 but I can't tell you specifically what --

25 Q. Okay, so you don't know that the

1 **dividend policies are the same among all the**
2 **peer group members in Spire?**

3 A. No. No. Sorry.

4 MR. MILLS: That's all I have.
5 Thanks.

6 JUDGE DIPPELL: Midwest Energy
7 Consumers?

8 MR. WOODSMALL: No questions.

9 JUDGE DIPPELL: Environmental
10 Defense Fund?

11 MS. KARAS: No questions.

12 JUDGE DIPPELL: Spire?

13 MR. FISCHER: Briefly.

14 RECROSS-EXAMINATION BY MR. FISCHER:

15 **Q. You had a question I think from the**
16 **Chairman about the board of directors --**

17 A. Yes.

18 **Q. -- of Spire Missouri and Spire Inc.**

19 A. (Nodding.)

20 **Q. Have you actually looked at who -- what**
21 **individuals are on those boards?**

22 A. It's been a little bit, but I did
23 review that. It's been about a couple weeks
24 ago.

25 **Q. Would it surprise you if you learned**

1 that Susan Sitherwood was on both boards?

2 A. That wouldn't surprise me.

3 Q. Would it surprise you that she's the
4 only joint director on both boards?

5 A. I'm not aware of that.

6 Q. There were some questions about, I
7 think, the financing requirements of the
8 subsidiaries Alagasco.

9 If the Alabama Public Service
10 Commission ordered Alagasco to have a hundred
11 percent equity ratios, should that affect
12 Missouri rates?

13 A. Well, that's a rate-making capital
14 structure. I don't know that it's going to
15 affect how they actually capitalize themselves.

16 Q. But would Staff want to include a
17 hundred percent equity coming from Alagasco with
18 the rate-making capital structure in the future?

19 A. Again, I'm not sure that the Company is
20 going to follow through and do a hundred percent
21 equity at the Company level, so that wouldn't be
22 included in a consolidated capital structure.
23 How they finance themselves would be.

24 Q. So if they were financed at a hundred
25 percent equity, they were ordered to do so by

1 **some other regulatory commission, that would**
2 **show up, correct?**

3 A. It would show up.

4 **Q. And should that from your perspective**
5 **be included in Missouri rates?**

6 A. I would want to review the
7 circumstances at the time as to whether or not
8 that was done for, you know, something that's
9 going on at the consolidated. Maybe Spire
10 Incorporated is issuing the debt for them. I
11 don't know.

12 **Q. Do you happen to know when Spire Inc.**
13 **made its last equity infusion into Laclede Gas**
14 **or Spire Missouri?**

15 A. I think I provide that example in my
16 testimony. It was in 2012.

17 **Q. Several years ago?**

18 A. Yeah, right before the last rate case.

19 **Q. Okay. I think you suggested the**
20 **Commission ought to look at the KCPL order as**
21 **far as benchmarking equity as guidance, correct?**

22 A. I think I generally expect them to look
23 at it as a benchmark, it is their order, yes.

24 **Q. Would you expect them also to look at**
25 **what they've done on short-term debt for capital**

1 **structure purposes for -- in KCPL?**

2 A. I don't think they have gas
3 inventories, but the -- there was a different
4 circumstance. I think they really need to
5 understand the details that with electric they
6 don't have gas inventories that have a carrying
7 charge. So I don't think it's appropriate for
8 them to look at that as a benchmark.

9 **Q. What about all the other public**
10 **utilities that don't have short-term debt in**
11 **their capital structure, should they look at**
12 **those?**

13 A. I think we need to look at what the
14 short-term assets are and what the carrying
15 charges should be for those.

16 **Q. Okay. And in those cases construction**
17 **work in progress often exceeds any short-term**
18 **debt, right?**

19 A. With electric, definitely from the
20 period from 2005 to 2012. There was a large
21 construction cycle during that period of time
22 for electricians.

23 MR. FISCHER: Judge, I think I may
24 have failed to move for the admission of
25 Exhibit 60, and if that's the case, I would do

1 so now. And that's all the questions I have.

2 JUDGE DIPPELL: Okay, Exhibit 60 was
3 the Staff accounting schedule from GR -- or a
4 portion of the Staff accounting schedules from
5 GR-2014-0007. Would there be any objection to
6 that exhibit?

7 (No response.)

8 JUDGE DIPPELL: Seeing none, then I
9 will admit that into evidence.

10 (SPIRE EXHIBIT NO. 60 RECEIVED INTO
11 EVIDENCE.)

12 JUDGE DIPPELL: And with that, I
13 believe that concludes your testimony for today,
14 Mr. Murray.

15 MR. THOMPSON: Do I get to do
16 Redirect?

17 JUDGE DIPPELL: Oh, I'm terribly
18 wanting to get him off the stand. Okay, one
19 more time, you can stay.

20 Redirect, Mr. Thompson?

21 MR. THOMPSON: Thank you, Judge.

22 REDIRECT EXAMINATION BY MR. THOMPSON:

23 **Q. Mr. Fischer asked you an extensive**
24 **series of questions. Do you recall those**
25 **questions?**

1 A. Yes.

2 Q. Okay. He asked you questions, if you
3 recall, about the Commission's order in
4 GR-2014-0086 having to do with Summit Natural
5 Gas of Missouri. Do you remember that?

6 A. Yes.

7 Q. Now, if you know, is Summit Natural Gas
8 a subsidiary of Spire?

9 A. No.

10 Q. Was it in 2014?

11 A. No.

12 Q. Did it have any particular relationship
13 to Spire?

14 A. Not that I'm aware of.

15 Q. Or to Laclede or Laclede Group?

16 A. No.

17 Q. And the recommendations that you made
18 in that case, were they based on the particular
19 facts that you became aware of pertaining to
20 Summit Natural Gas's financial situation?

21 A. Yes. They're an expanding company in
22 areas that have propane and they're trying to
23 penetrate those markets, so it's almost -- it's
24 almost a bit competitive, to be honest with you.

25 Q. And are the circumstances that existed

1 that led you to make the recommendations that
2 you did in Case GR-2014-0086, are those same
3 circumstances, do they apply today to Spire
4 Missouri?

5 A. No.

6 Q. Is Spire Missouri's circumstance, would
7 you characterize it as significantly different?

8 A. Significantly different because Summit
9 Natural Gas Missouri is trying to even just earn
10 a positive profit. I mean, they're barely -- I
11 mean, they're not doing the best and actually
12 they've had -- I know from doing finance cases
13 on Summit Natural Gas in Missouri that they wish
14 to have -- to termed out their long-term debt
15 and have been unable to do so because their
16 financial performance is not the best due to
17 expanding into areas where there's never been
18 any natural gas and, you know, competition with
19 propane and electric.

20 Q. So in your professional opinion as a
21 financial analyst, is there any logical relation
22 between the recommendations you gave in Case
23 GR2014-0086 and the present case?

24 A. Well, no. And I would just like to
25 point out that actually the 40/60 percent

1 capital structure Staff recommended was the
2 Company's targeted capital structure that they
3 wanted to achieve, but because their financial
4 performance was not as what they had hoped it
5 would be, you know, this is what the creditor
6 said, you have to keep this capital structure
7 more equity rich.

8 **Q. And I appreciate that explanation, but**
9 **does that have any rational relationship to the**
10 **Company that's in front of the Commission in**
11 **this case?**

12 A. They're different risk profiles.

13 **Q. Thank you.**

14 **And if I were to ask you the same**
15 **questions about Case GR-2014-0152, would your**
16 **responses be substantially the same?**

17 A. I'm sorry, repeat your question. I was
18 looking at --

19 MR. THOMPSON: I'm trying to speed
20 this up, Judge.

21 THE WITNESS: Sorry.

22 JUDGE DIPPELL: Appreciate it.

23 BY MR. THOMPSON:

24 **Q. Is there any rational relationship in**
25 **your mind between the circumstances of Liberty**

1 **Utilities' Midstates Gas Corporation in 2014 and**
2 **those of Spire Missouri in 2017?**

3 A. The capital structure I do believe
4 is -- there is some importance there because of
5 the fact that Liberty Utilities issued all of
6 the debt on behalf its gas operations and its
7 electric operations. The Commission found the
8 consolidated holding company capital structure
9 to be appropriate, which had 45 percent equity
10 in it.

11 Q. Okay. Was Liberty Utilities at that
12 time, was that part of the Laclede Group?

13 A. No.

14 Q. Is it a subsidiary of Spire today?

15 A. No.

16 Q. And so were your recommendations in
17 that case, were they driven by circumstances
18 that are similar to the circumstances in the
19 present case?

20 A. No.

21 Q. Is there -- so, again, in your
22 professional opinion as a financial analyst, is
23 there any logical, rational relationship between
24 the recommendations you gave in this case in
25 2014 and those you have given in the present

1 **case in 2017?**

2 A. I think it's important to evaluate the
3 trend in capital costs, and I think that that's
4 what I've done since 2014.

5 Q. Okay. So you think there's an
6 illustrative --

7 A. Yes.

8 Q. -- aspect that might be helpful to the
9 Commission?

10 A. Yes.

11 Q. Okay. I'll accept that.

12 And with respect to case GR-2014-0007,
13 I think we were asked to look at a page out of
14 Staff's accounting schedule to see to our
15 surprise that there is no short-term debt in
16 that capital structure. Do you see that?

17 A. It wasn't to my surprise, but...

18 Q. Is there a reason why there was none in
19 that case, but you are recommending it in this
20 case?

21 A. Yes, the circumstances have definitely
22 changed. There was no -- there were no -- there
23 wasn't any gas inventories in rate base at that
24 period of time. So if -- you know, just like
25 looking at the 53.56 percent equity ratio, that

1 would look unreasonable at its face, but if you
2 imputed 10 percent of short-term debt in here,
3 that would lower your equity ratio to 47, 48
4 percent. And, you know, that is very important
5 because even though the short-term debt isn't in
6 this capital structure, we are, you know,
7 through what we had done in the past or what
8 have been doing right now, actually, where we
9 allow, you know, carrying costs based on the
10 short-term debt rate, that is based on the
11 presumption that all parties agreed to that
12 this -- that because gas inventories are
13 short-term assets, short-term interest rates
14 should be applied.

15 **Q. So if I understand you, are you saying**
16 **that the treatment of short-term debt that you**
17 **recommend varies from case to case based on the**
18 **circumstances of the case?**

19 A. Yes.

20 MR. PENDERGAST: Your Honor, one of
21 the issues in this case is whether we should
22 have LEC's -- Laclede's storage inventories
23 included in base rates as MGE's storage
24 inventories are included in base rates.

25 Since that's an issue that all the

1 parties have recognized and since it establishes
2 that storage inventories are included in MGE's
3 base rates, I think that correction needs to go
4 on the record.

5 JUDGE DIPPELL: I didn't quite
6 follow you, Mr. Pendergast. I'm sorry.

7 MR. PENDERGAST: It's just
8 Mr. Thompson asked a question: Why was there
9 no short-term debt in MGE's case? And the
10 answer was: Because it doesn't have storage
11 inventories in base rates.

12 And I'm just saying the official issues
13 in this case have the issue of whether or not
14 LEC's case inventories should be in base rates
15 like MGE's storage inventories are on base
16 rates -- or in base rates.

17 JUDGE DIPPELL: I understand now. I
18 wasn't sure -- I didn't recall that that was the
19 MGE that was...

20 Mr. Thompson, were you -- did you have
21 other questions?

22 MR. THOMPSON: Oh, I do.

23 JUDGE DIPPELL: Okay.

24 MR. THOMPSON: Thank you.

25

1 BY MR. THOMPSON:

2 Q. Now, Mr. Murray, you were asked
3 questions about increases to the Fed fund's
4 rates. Did I say that right? It's like Peter
5 Piper, it's hard to say.

6 A. Yes.

7 Q. Fed fund's rate?

8 A. Yes. That's an abbreviation.

9 JUDGE DIPPELL: Mr. Thompson, your
10 microphone, you're getting farther and farther
11 away.

12 MR. THOMPSON: I apologize, Judge.

13 BY MR. THOMPSON:

14 Q. You agreed that those have increased
15 several times; isn't that correct?

16 A. Yes.

17 Q. And, in fact, the Fed is contemplating
18 raising them again; isn't that true?

19 A. Yes.

20 Q. Have long-term interest rates increased
21 significantly over the past few quarters?

22 A. No.

23 Q. So the rise in the Fed fund's rate is
24 not significant for long-term interest?

25 A. That's correct. There's actually a

1 flattening of the yield curve right now.
2 Short-term rates are coming up, long-term rates
3 haven't moved, so there's not much of a spread
4 between two years and ten years.

5 Q. Okay. Now, let's talk about the
6 operations of a holding company and a group of
7 subsidiaries. That's what we have in this case;
8 isn't that's correct?

9 A. Yes.

10 Q. When Laclede borrows money -- and I'm
11 talking about the holding company. Let's just
12 call it "the holding company."

13 When Spire borrows money, is it or is
14 it not borrowing money on the strength of the
15 cash flows from the operating companies?

16 A. Yes.

17 Q. And if Spire carries a significant
18 quantity of debt in its capital structure, does
19 that have an effect of raising the cost of
20 capital for the operating companies?

21 A. Yes.

22 Q. And, in fact, the operating companies
23 are rated lower than the holding company; isn't
24 that correct?

25 A. No, that's --

1 Q. In terms of bond ratings. Isn't that
2 what you testified?

3 A. No, the utility subsidiaries for S&P,
4 it's rated all the same as far as the corporate
5 credit rating. For Moody's, the -- Spire is
6 rated two or three notches -- two notches lower
7 than --

8 Q. Two notches lower, okay.

9 A. As compared to Spire Missouri.

10 Q. I see. So I had that backwards.

11 Thanks for straightening that out.

12 Nonetheless, if Spire decides to make
13 another acquisition, for example -- and they've
14 made several in the past few years; isn't that
15 correct?

16 A. Yes.

17 Q. So let's say they want to make another
18 one. And they would raise, let's say, a mix of
19 equity and debt to pay for it, correct? You
20 with me?

21 A. Yeah, that would be consistent with
22 what they have done in the past, yes.

23 Q. Okay. Would that have the effect of
24 raising the cost of capital for Spire Missouri?

25 A. Depends on how they capitalize it. I

1 mean, if they capitalize it with more equity
2 just like -- say, for instance, they were able
3 to find a merger of equals and they just did
4 stock-for-stock swap, no additional debt at the
5 holding company, and it was a better -- it was a
6 low risk operation, another, you know, I guess
7 gas distribution operation somewhere else and --
8 but no additional financial risk. That could
9 actually help improve it. It depends on how
10 they finance it.

11 **Q. It depends how they do it?**

12 A. Exactly.

13 **Q. Okay. Well, let's say it's heavily**
14 **leveraged. What would the effect be in your**
15 **opinion?**

16 A. That would continue to suppress the
17 credit ratings at the subsidiary level.

18 **Q. And would that mean that Missouri**
19 **ratepayers would be paying more?**

20 A. Yes.

21 **Q. Now, the Chairman asked you about the**
22 **principles that the Commission should use to**
23 **determine the capital structure issue. Do you**
24 **remember those questions?**

25 A. Yes.

1 Q. And those principles in fact have to do
2 with the effect of holding company leverage on
3 the operating company; is that right?

4 A. Yes.

5 Q. When you spoke about ringfencing, what
6 did you mean?

7 A. Ringfencing is definitely much more
8 involved than just a few conditions in the
9 stipulation and agreement. I think there has to
10 be significant structural and legal mechanisms
11 put in place that has buy-in from the Company,
12 that has enforcement ability from the
13 Commission, that there might be penalties if
14 they violate those.

15 I mean, that's where Wisconsin, because
16 of their legislature, they made it -- you know,
17 that you could be charged if you violated
18 certain conditions that did not continue to
19 allow the safety of the utility operations and
20 the financing of those operations.

21 Q. Okay. So let me make sure I
22 understand. Ringfencing would -- does that
23 refer to a situation where legally and
24 financially the operating company is separated
25 from the holding company to such a degree that

1 **they're regarded as separate entities, so that**
2 **what happens to one will not necessarily affect**
3 **the other?**

4 A. Well, I think -- they're already
5 separate entities.

6 **Q. Okay.**

7 A. It's whether or not somebody is
8 actually looking out for the best interest of
9 that subsidiary, and that's why many times
10 you'll have an independent director that has --
11 basically has no interest and has not been part
12 of the management of either company for sometime
13 and that's their sole -- I mean, they could
14 basically have a veto privilege of any action
15 that may be taken that may be -- you know, cause
16 financial harm to that subsidiary.

17 **Q. So in your opinion, is there effective**
18 **ringfencing between Spire Missouri and Spire?**

19 A. Again, I don't think my opinion's the
20 most important on this. I think it's the rating
21 agency's, but no.

22 **Q. You're the one on the stand.**

23 A. I know and I understand that, but the
24 investors' opinions are most important, and I am
25 trying to say what investors think.

1 Q. And what do they think?

2 A. They do not see that there's effective
3 ringfencing.

4 Q. Okay. Now, after all these questions
5 from me and from other people, you agree that
6 your recommendation continues to be 9 to 9.5?

7 A. Yes.

8 Q. A midpoint of 9.25?

9 A. Yes.

10 Q. Have you heard anything that would lead
11 you to move away from that?

12 A. No.

13 Q. Now, you do believe that that's
14 significantly higher than the actual cost of
15 equity, don't you?

16 A. Yes.

17 Q. What's the effect of awarding ROEs to
18 companies that are significantly higher than
19 their actual cost of equity?

20 A. It continues to support higher
21 market-to-book ratios. I mean, to the extent
22 that -- to the extent that, you know, they are
23 able to invest in projects where they earn more
24 than their cost of equity, that creates
25 shareholder value. I mean, that's the

1 fundamental economic principle between -- you
2 know, as far as trying to set the allowed return
3 equivalent to the of cost of equity is that any
4 ongoing investment, you know, will not cause the
5 shareholder to be better off or worse off.

6 But to the extent that you have, you
7 know, let's say a margin of 225 basis points of
8 allowable return over the cost of equity, I
9 mean, obviously that encourages additional
10 investment because to the extent that they are
11 able to do so, that expected return over the
12 discount rate creates more value, present value
13 of those cash flows.

14 **Q. Okay. You said that the shareholders**
15 **are better off. What about the ratepayers? Are**
16 **they better off?**

17 A. Depends on if they're trying to
18 preserve any of that cash at the subsidiary for
19 investment in that stand-alone entity.

20 I mean, I think it may be more
21 acceptable in my opinion to allow a margin over
22 the cost of equity if you know that those cash
23 flows are going to stay with the utility and
24 benefit the financial soundness of that
25 subsidiary.

1 MR. THOMPSON: I have no further
2 questions. Thank you, Judge.

3 JUDGE DIPPELL: Thank you,
4 Mr. Thompson.

5 I think third time is the charm.

6 THE WITNESS: Thank you.

7 JUDGE DIPPELL: And that you may
8 step down, Mr. Murray.

9 THE WITNESS: Thank you.

10 (Witness excused discussed at 3:33 p.m.)

11 JUDGE DIPPELL: Okay. It's getting
12 late in the afternoon and we're going to take a
13 short break. But before we do, I just want to
14 clarify my ruling on the official notice.

15 So I've taken a look at the statute
16 and, yes, Mr. Woodsmall, that is in fact
17 evidence and the facts for which we are taking
18 notice are those which were discussed with
19 Mr. Murray on the stand and the general premise
20 that that is an action that the Commission took
21 in those other cases and the weight of that is
22 what the Commission has to weigh.

23 But in answer to your question --

24 MR. WOODSMALL: Thank you.

25 JUDGE DIPPELL: -- does that change

1 your objection of relevance or add any other
2 objections?

3 MR. WOODSMALL: No. Your -- no.

4 JUDGE DIPPELL: Does that add other
5 objections?

6 MR. WOODSMALL: No.

7 MR. MILLS: Judge, just to clarify,
8 you're taking official notice of those portions
9 of the reports and orders that were read into
10 the record? You're not taking the entire case
11 record?

12 JUDGE DIPPELL: No, not the entire
13 case record. Just the report and order, the
14 testimony that Mr. Murray gave about his
15 opinions and the actions that the Commission
16 took in that case.

17 MR. MILLS: Okay. Great. Thank
18 you.

19 JUDGE DIPPELL: Okay. With that
20 then, we will take a break for 15 minutes.
21 Please come back, if I can do my math, at ten
22 'til, ten 'til 4.

23 We can go off the record.

24 (Recess taken from 3:33 p.m.
25 to 3:51 p.m.)

1 JUDGE DIPPELL: Let's go back on the
2 record. Okay, we're going back on the record.

3 And before we went back on the record,
4 there were a few minor scheduling issues we
5 discussed that MIEC's witness Greg Meyer need
6 not come both Tuesday and Thursday, but we'll do
7 the Cross-Examination on both of his issues on
8 Thursday.

9 And the Environmental Defense Fund
10 witness is only available on the 13th, correct?

11 MS. KARAS: Yes.

12 JUDGE DIPPELL: So we'll make sure
13 to get that witness on that date.

14 Okay. I think we are ready to finish
15 up this with Mr. Gorman.

16 MR. MILLS: Yes, OPC and MIEC call
17 Mr. Michael Gorman.

18 (Witness sworn.)

19 THE WITNESS: I do.

20 JUDGE DIPPELL: Now, before we begin
21 I should have gone through one more procedural
22 issue with regard to Mr. Gorman. Since this is
23 a witness that is sponsored by both MIEC and
24 OPC, how is the direct going forward?

25 MR. MILLS: Mr. Smith will do

1 direct, the brief introductory direct, and then
2 for Redirect, we both would like to conduct
3 Redirect.

4 JUDGE DIPPELL: Would there be any
5 objection to that occurring?

6 (No response.)

7 JUDGE DIPPELL: All right. Then
8 that is the procedure that we will follow.

9 So go ahead, Mr. Smith.

10 MR. SMITH: Thank you.

11 MICHAEL GORMAN testified as follows:

12 DIRECT EXAMINATION BY MR. SMITH:

13 Q. Good afternoon, Mr. Gorman.

14 A. Good afternoon.

15 Q. Would you please state and spell your
16 name for the court reporter?

17 A. My name is Michael
18 Gorman, M-I-C-H-A-E-L G-O-R-M-A-N.

19 Q. And by whom are you employed?

20 A. Brubaker & Associates.

21 Q. Did you prepare or cause to be prepared
22 a Direct testimony --

23 A. I did.

24 Q. -- Rebuttal testimony, Surrebuttal
25 testimony in both cases, GR-2017-0215 and

1 GR-2017-0216?

2 A. Yes.

3 Q. OPC has copies of those items which
4 have been premarked as Exhibits 407, 414 and
5 44 -- sorry, 416.

6 JUDGE DIPPELL: And those are also
7 the numbers that I had.

8 BY MR. SMITH:

9 Q. And, Mr. Gorman, do you have your
10 testimony in front of you?

11 A. I do.

12 Q. Do you have any corrections to make to
13 that testimony?

14 A. I do not.

15 Q. If I were to ask you the same questions
16 that appear in your testimony, would your answer
17 be the same or substantially the same?

18 A. Yes.

19 MR. SMITH: This will be
20 Mr. Gorman's only issue that he'll be testifying
21 on, and so at this time I would offer those
22 exhibits into the record.

23 JUDGE DIPPELL: Would there be any
24 objection to Exhibits 407, 414 and 416?

25 MR. PENDERGAST: None here.

1 JUDGE DIPPELL: Seeing no
2 objections, I will admit those into the record.

3 (OPC EXHIBIT NOS. 407, 414 AND 416
4 RECEIVED INTO EVIDENCE.)

5 MR. SMITH: OPC tenders Mr. Gorman
6 for Cross-Examination.

7 JUDGE DIPPELL: Is there
8 Cross-Examination by Staff?

9 MR. THOMPSON: No questions. Thank
10 you, Judge.

11 JUDGE DIPPELL: Midwest Energy
12 Consumers?

13 MR. WOODSMALL: Yes, just briefly to
14 clarify a couple of things from earlier.

15 CROSS-EXAMINATION BY MR. WOODSMALL:

16 **Q. What is Spire's -- Spire Inc.'s credit**
17 **rating?**

18 A. That's actually shown on one of my
19 schedules to my direct testimony.

20 As shown on my Schedule 1PG3 to my
21 direct testimony, Spire Inc. has an A- bond
22 rating from S&P and an AA2 rating from Moody's.

23 **Q. And do you know what the Ameren and**
24 **Great Plains credit ratings are?**

25 A. Yes. Ameren has a BBB+ bond rating

1 from S&P and BAA1 bond rating from Moody's.
2 That would be a weaker bond rating than Laclede
3 Gas Company or Spire Missouri. KCP&L has a BBB+
4 bond rating from S&P and BAA1 bond rating from
5 Moody's.

6 **Q. And just so I understand, if Spire has**
7 **a higher credit rating than investors, all else**
8 **being equal, then investors would require a**
9 **lower return on equity; is that correct?**

10 A. Yeah, a higher bond rating is an
11 indication of lower investment risk for both
12 debt -- in equity investments and an indication
13 of lower investment risk would -- it would be
14 appropriate to have a lower return on equity.

15 **Q. The second question: Ms. Ahern was**
16 **saying that regulatory climate is large concern**
17 **in the credit rating or consideration. Maybe**
18 **"concern" is the wrong word.**

19 **Can you tell me how credit rating**
20 **agencies view the Missouri regulatory**
21 **environment for Spire Missouri?**

22 A. Well, she's -- I agree that it is a
23 significant concern, and to her Rebuttal
24 testimony she attaches credit rating reports
25 from both Moody's and S&P for Spire, and in both

1 of those report, it refers to the Missouri
2 regulatory environment for Spire Inc. and
3 Laclede Gas specifically as supportive. So that
4 the regulatory treatment for this utility has
5 supported strong credit standing.

6 **Q. And final question: Can you tell me in**
7 **your view what authorized rates of return have**
8 **done since 2014?**

9 A. That also is shown on average on a
10 couple of my schedules. One of them Schedule
11 1PG12 for gas utilities. In 2014, the average
12 authorized return on equity for a gas LDC was
13 around 9.78. Through the first six months of
14 2017 that dropped down to about 9.5.

15 Subsequent to me filing this testimony
16 the third quarter report for 2017 was made
17 available. The average for the first three
18 quarters is around 9.8 percent, but there are
19 two rate decisions in there that are notable
20 outliers that increase the average for the LDCs
21 in the industry. One of them was for an Alaskan
22 gas utility where the Commission ordered a
23 return on equity of approximately 11.9. I think
24 it was 11.88 specifically.

25 And then Piedmont also had an

1 authorized return on equities of about
2 10.2 percent. And that's a company that has
3 some financial difficulties in the consolidated
4 enterprise. And I don't know if the South
5 Carolina Commission considered those financial
6 difficulties for that company in awarding return
7 on equity, but they do exist.

8 Except for those two notable exceptions
9 in the third quarter of this year, the
10 authorized returns on equity for gas utilities
11 and even electric utilities have been relatively
12 flat over the last 18 to 24 months.

13 MR. WOODSMALL: No further
14 questions. Thank you.

15 JUDGE DIPPELL: Anything from the
16 Environmental Defense Fund?

17 MS. KARAS: No questions, your
18 Honor.

19 JUDGE DIPPELL: Spire?

20 MR. PENDERGAST: Thank you.

21 CROSS-EXAMINATION BY MR. PENDERGAST:

22 Q. Good afternoon, Mr. Gorman.

23 A. Good afternoon.

24 Q. I understand you just got back from
25 Alaska?

1 A. I did, yes.

2 Q. Was that higher return you referenced
3 from Alaska your handy work?

4 A. It was not.

5 Q. It was not.

6 Let me ask you: When Laclede acquired
7 MGE in 2013, would you agree with me that that
8 was financed with roughly equal amounts of debt
9 and equity?

10 A. When they acquired the total company,
11 that's -- yes, I would agree with that.

12 Q. Okay. And do you -- you've worked on a
13 number of Laclede cases before; is that correct?

14 A. I think that's a fair characterization,
15 yes.

16 Q. Okay. And do you have a sense for
17 Laclede, what sort of equity component it had in
18 prior cases?

19 A. Its requested equity component, yes,
20 it's been well above 50 percent. I would have
21 to look at past records to nail that down more
22 specifically.

23 Q. Okay. And to your knowledge, to the
24 extent you remember, has that been for some
25 time? Has that extended over a significant

1 **period of time?**

2 A. I think, yeah, consistently they have
3 relied on Laclede Group, the parent company's
4 capital structure and the recommended positions.

5 I have consistently recommended the
6 utility-specific capital structure. Utility
7 consistently opposed me in all cases up 'til
8 this one, so I think that's kind of a -- from a
9 high level of the review that's taken place
10 historically.

11 **Q. And can you tell me why you recommended**
12 **the utility-specific capital structure?**

13 A. Because I think the objective of
14 setting rates for utility is to set price and I
15 think the price is important.

16 When you set a utility price, it gives
17 utility customers a signal on what the cost of
18 utility service is, but it also sets discipline
19 for utility management. The regulatory body
20 says this is the price we have to manage our
21 cost to to allow us to earn our authorized
22 return on equity within the price, the
23 parameters of the pricing discipline created by
24 that regulatory body.

25 If you set the cost of service

1 consistent with utilities, actual financial
2 statements and the information that they publish
3 that represents what their cost to providing
4 utility service is and prices are set, that
5 gives clear direction to utility management that
6 certain costs may be excessive and need to be
7 reduced, other areas of the operation may need
8 to be broadened and expanded consistent with the
9 pricing structure approved by the regulatory
10 commission.

11 So from that standpoint, I think it's
12 important in setting utility prices that both
13 customer and utility management get clear
14 information and clear objectives from what the
15 price-setting authority believes is appropriate
16 cost structure for providing utility service.

17 **Q. Thank you. Is it fair to say that your**
18 **analysis or the scope of your work in this**
19 **proceeding was limited primarily to return on**
20 **equity and capital structure?**

21 A. Overall rate of return, yes.

22 **Q. Yes.**

23 A. Yes.

24 **Q. Yes, overall rate of return.**

25 **And would it also be fair to say that**

1 you didn't attempt to undertake an analysis of
2 the acquisitions that have been made by either
3 Spire or Laclede Gas Company in terms of the
4 synergies that they have produced?

5 A. Well, I did review the Company's
6 testimony concerning its cost of service in this
7 case and I do understand that they believe that
8 certain synergies or cost savings have been
9 realized as a result of the acquisition.

10 Q. Okay. But you didn't do an independent
11 analysis of that on your own other than
12 reviewing maybe what the Company filed?

13 A. Yeah, that's -- I did review what the
14 Company's filing has been in terms of what the
15 cost savings would be, the cost to achieve, and
16 I did not dig further into that issue than to
17 review the Company's position.

18 MR. PENDERGAST: Okay, great. Thank
19 you very much. I have no further questions.

20 JUDGE DIPPELL: Are there any
21 questions from the Bench for Mr. Gorman?

22 CHAIRMAN HALL: Yeah.

23 QUESTIONS BY CHAIRMAN HALL:

24 Q. Good afternoon.

25 A. Good afternoon.

1 Q. I'm going to ask you one of the
2 questions I asked Mr. Murray, and that is:
3 When the Commission is making a capital
4 structure determination between a subsidiary
5 only or a consolidated capital structure, what
6 do you think is the most important criteria or
7 principles that we should take into account?

8 A. Well, ideally it would be the
9 utility-specific capital structure, and then the
10 determination would be whether or not the
11 utility's effectively managing that capital
12 structure so as to maintain its financial
13 integrity, credit standing, but to do that at
14 the lowest possible costs to retail customers.

15 And that's how I approach my review of
16 Laclede's actual capital structure, and I found
17 that without removing goodwill, the common
18 equity ratio was much higher than needed in
19 order to support their current bond rating.
20 Consequently, I found their proposed capital
21 structure was unreasonable because it contained
22 an excessive amount of common equity.

23 And as I alluded to earlier, I think
24 focusing --

25 Q. Well, let me stop you there for a

1 second because -- so you looked at the numbers
2 and determined whether or not the numbers were
3 reasonable, and if the numbers were not
4 reasonable -- and if they are not reasonable,
5 then you propose some deviation from the
6 standard course of a utility-specific capital
7 structure; is that correct?

8 A. It's very close to correct. I looked
9 at their position and I first asked: Is this
10 the actual capital structure that represents the
11 debt and equity capital actually used to make
12 investment in utility plant and equipment?

13 In that first step, I concluded that it
14 was not because on the utility's balance sheet
15 is a goodwill asset, and for the reasons
16 outlined in my testimony, goodwill cannot be
17 supported by debt capital because it doesn't
18 produce cash flows. It would be imprudent for
19 the utility to issue debt to fund a goodwill
20 asset. If they did, it would have wrote their
21 credit standing.

22 So when I asked the question whether or
23 not the utility's proposed capital structure
24 actually represents the debt and equity used to
25 support their investment in utility rate base

1 assets, my conclusion was, no, it's not because
2 it includes common equity that supports a
3 goodwill asset.

4 When I adjust it, the capital
5 structure, to remove the common equity
6 supporting the goodwill asset, I arrived at what
7 I believe to be the utility's actual mix of debt
8 and equity capital used to support their
9 investment in the utility rate-based assets.

10 And based on that determination, at the
11 original filing the Company requested a 57
12 percent common equity ratio, I found that it
13 would be appropriate to reduce the common equity
14 ratio or the common equity balance by about
15 \$210 million and to reflect their plan to
16 refinancing assumed short-term debt with
17 long-term debt. And with those two adjustments,
18 I got a utility capital structure about
19 47 percent equity and 53 percent debt, and that
20 was the capital structure I believe the utility
21 uses to finance investment in utility plant and
22 equipment.

23 My next question then was: Is that
24 capital structure and is the Company's capital
25 structure reasonable for rate-making purposes?

1 And in that evaluation, I asked the question
2 whether -- what is a reasonable capital
3 structure, what does maintain financial
4 integrity and credit standing at the lowest
5 possible cost to customers?

6 And in that second analysis, I again
7 rejected the Company's actual capital structure
8 because it contains too much common equity. In
9 that second analysis, I found that my adjustment
10 to the Company's capital structure has a
11 relatively thin amount of common equity, but
12 still reasonably consistent with what we're
13 seeing for other utilities and supporting their
14 bond rating in -- around the country.

15 **Q. Did you consider other possible**
16 **adjustments other than the 210 million goodwill**
17 **adjustment?**

18 A. Well, there's two adjustments. One was
19 their planned -- plan to refinance about
20 \$170 million of short-term debt to long-term
21 debt and to remove the goodwill.

22 I didn't look at any other adjustments
23 beyond that because --

24 **Q. The first one has been agreed to by the**
25 **Company, correct?**

1 A. It has.

2 Q. Okay. So it's only the second one
3 that's at issue now?

4 A. Yes. And I didn't look further to
5 adjust the capital structure because I found
6 that once you remove the common equity
7 supporting goodwill, the resulting capital
8 structure, it's a little light on common equity,
9 but it's reasonable for rate-making purposes. I
10 concluded that it will support their financial
11 integrity, will support their bond rating, but
12 will do so at a much lower cost to retail
13 customers.

14 Q. Have you ever advocated for such an
15 adjustment before any other commission in any
16 other state?

17 A. Yes, I have, on several occasions. In
18 Illinois -- right now in Illinois, there's a law
19 that says you have to adjust the capital
20 structure the way I'm proposing here if a
21 utility has an acquisition adjustment of
22 goodwill on their balance sheet.

23 But before the law was changed, we
24 addressed this issue with respect to
25 Commonwealth Edison, and the Commission -- and

1 the resulting adjustment to the capital
2 structure moved their goodwill -- or their
3 capital structure from about 60 percent equity
4 down to less than 40 percent equity. The
5 Commission found that the Company's proposed
6 capital structure was unreasonable because the
7 common equity ratio was too high, but it felt
8 that my capital structure wasn't reasonable
9 because the common equity ratio was too low, so
10 it imputed a common equity ratio and debt ratio
11 in setting rates in that case.

12 Subsequent to that, you know, some laws
13 changed in Illinois and a formula rate-making
14 process was implemented for electric utilities
15 and largely based on the significant issues in
16 my judgment -- you know, I'm not sure what
17 happened at the legislature, but I do know that
18 the law changed right after this issue we had
19 with Commonwealth Edison's capital structure.

20 In the Commission's finding that it
21 would be appropriate to make that kind of
22 adjustment to a rate-making cap structure to
23 remove goodwill from common equity, the
24 legislature mandated that in the formula rate
25 process, when you develop a capital structure to

1 use in that formula, common equity will be
2 adjusted to remove the common equity supporting
3 goodwill. So now that's the rate-making
4 practice in Illinois.

5 I was also in a Federal Energy
6 Regulatory Commission with respect to Niagra
7 Mohawk and there was suggestions of -- the New
8 York Public Service Commission, they had made a
9 goodwill adjustment to the capital structure.
10 As a result, it was a settled process at the
11 FERC, but part of that settlement did reflect a
12 compromise on capital structure.

13 So there wasn't an explicit finding on
14 that, but there was a willingness by the utility
15 to adjust their capital structure rate-making --
16 to form a rate-making one that didn't reflect
17 all the common equity supporting goodwill.

18 I would also point out that most
19 recently in most of the acquisition cases I've
20 been involved in, for example, Exelon's
21 acquisition of PHI, big utilities out East,
22 there was explicit statements by the utility
23 that the goodwill asset would not be included in
24 rate base and also the goodwill asset would be
25 reported at the parent company's cap structure

1 so it wouldn't impact the utility's cap
2 structure.

3 The same thing was offered by GPE in
4 its proposed acquisition of Westar, where if a
5 goodwill asset will be recorded, it will be
6 recorded at the parent company level, not at the
7 operating utility's subsidiary. So that seems
8 to be more of the trend now in order to ensure
9 that no cost associated with a transaction, the
10 creation of a goodwill asset will actually be
11 included in the rate-making process.

12 Q. Okay. Thank you.

13 Concerning Staff's analysis with
14 regards to the ROE recommendation --

15 A. Um-hum.

16 Q. -- Staff essentially, my understanding,
17 is proposing that we look at two prior -- our
18 last two major utility rate cases in Ameren/KCPL
19 where we determined that a 9.5 ROE was
20 appropriate or approximately and then use that
21 as a benchmark and then look at what's happened
22 since then and decide which way we should
23 perhaps adjust that 9.5.

24 Is that essentially your understanding
25 of Staff's analysis and recommendation?

1 A. It is, but then I think it's important
2 -- and Mr. Murray also looked at what he
3 thought to be the current market cost of equity.
4 So when he implemented that procedure, he didn't
5 result in an ROE -- recommended ROE that was
6 less than the utility's cost of equity.

7 And I think that's important because
8 Hope and Bluefield standard says an awarded ROE
9 has to be fair compensation, also maintain
10 financial integrity and support the bond rating.

11 **Q. Right. So --**

12 A. I do think that was a significant first
13 step that he undertook to recommend his return
14 on equity.

15 **Q. So do you think that that is a proper**
16 **analysis?**

17 A. Well, I understand why he did it, but I
18 prefer to do the analysis the way I'm -- I do it
19 because I look at a lot of financial metrics to
20 try to gauge what the current market cost of
21 equity is, cost of capital is and what the
22 independent market participants believe capital
23 costs will be at least over the next two or
24 three years as that reasonably reflects the
25 period rates will be in effect.

1 And using that information and informed
2 judgment -- I've been doing this for about
3 30 years now -- is largely what I rely on in
4 order to form my recommended return on equity.
5 But at the same time, similar to what
6 Mr. Murray has done, I also look at
7 commission-authorized returns on equity for
8 every utility companies and I observe how the
9 market responds to those authorized returns on
10 equity.

11 And if the market responds in such a
12 way that the utility does have access to
13 capital, the securities of the utility are still
14 well received in the marketplace, I think that
15 is observable market evidence that the awarded
16 return on equity has been embraced as fair by
17 market participants.

18 **Q. So how did the market react to the 9.5**
19 **ROE that this Commission issued in the Ameren**
20 **and KCP&L cases?**

21 A. Well, I can't tell you specifically,
22 but the reaction to the security prices after
23 those rate decisions has been very robust.
24 Their equity shares are much higher now than
25 they've been at any time in history and, you

1 know, on a share divided basis their credit
2 ratings are quite strong, their ability to issue
3 debt at very low interest rates and plentiful
4 amounts of capital are very strong right now.

5 I think all the market -- observable
6 market evidence shows that the 9.5 was well
7 received by market participants.

8 CHAIRMAN HALL: I think that's all I
9 have. Thank you.

10 THE WITNESS: Thank you.

11 JUDGE DIPPELL: Any other questions?

12 COMMISSIONER RUPP: I have some
13 questions.

14 JUDGE DIPPELL: Commissioner Rupp.

15 COMMISSIONER RUPP: Thank you.

16 QUESTIONS BY COMMISSIONER RUPP:

17 **Q. Good afternoon, sir.**

18 **A. Good afternoon.**

19 **Q. I'm sure you took a look at**
20 **Mr. Hevert's comments about your testimony, and**
21 **one of the things that he was stating is that**
22 **it's not possible to trace, you know, specific**
23 **portions of the acquisition financing back to**
24 **specific assets as you had kind of suggest when**
25 **it comes to goodwill. Can you respond to that**

1 **comment?**

2 A. I can. In virtually every respect I
3 would agree with it with one exception, and
4 that's the purchase accounting used in a merger
5 transaction.

6 When one utility buys another, you
7 combine their assets together. You literally
8 add the assets, you add the liabilities, you
9 create a goodwill asset. In order to keep the
10 liabilities and asset in balance, they write up
11 common equity to keep the balance sheet in
12 balance. So when they create the paper goodwill
13 asset, they also create a paper amount of common
14 equity as part of -- as normal GAAP-related
15 purchase accounting. So that's the one instance
16 where I disagree with him because of simply the
17 accounting mechanisms used when two companies
18 merge together.

19 In virtually all other aspects of
20 making investments by utilities I agree, you
21 cannot trace capital to the assets used. But
22 that's not the case with purchase accounting.
23 It's very clear what occurs when two companies
24 combine their operations together and the
25 GAAP-reported accounting mechanisms that allow

1 for tracing of the creation and the creation of
2 the goodwill asset, at the same time writing up
3 their common equity balance.

4 Q. Okay, thank you. That helped.

5 And then he also states that you
6 mistakenly assume that equity investors would be
7 satisfied with investing in an asset that
8 produces no economic value, and then he states
9 that that wouldn't be true.

10 A. Well, that's simply wrong on its face.
11 And let me give you an example. Spire's stock
12 right now is trading at about 170 percent of its
13 book value. If you or I wanted to buy Spire
14 stock, we could not buy it at its book value.
15 We'd have to buy it at the market price, and the
16 market price, again, is a significant premium to
17 book value. All the earnings and cash flow that
18 would be available to that share of stock would
19 be based on the book value of the equity that is
20 used to invest in utility plant and equipment.

21 The difference between market price and
22 book value is not part of the cost of service
23 equations at the rate-making level. So it's
24 normal for investors to be willing to pay prices
25 that exceed book value when they take ownership

1 of the utility shares, more individually, or if
2 they're buying the utility itself in the case of
3 Laclede buying MGE. It's a normal transaction
4 to pay a price in excess of the book value
5 because that's the going market value of those
6 assets. But that doesn't mean that after
7 Laclede buys MGE, the customers of MGE have to
8 pay more to support that higher price.

9 As a matter of fact, that's something
10 regulatory commissions particularly protect
11 customers against happening after an
12 acquisition. In order to do that, there has to
13 be a commitment by the utility, which there was
14 in this case, that no costs associated with that
15 premium paid for MGE by Laclede would have the
16 effect of increasing the utility's cost of
17 service if the transaction was completed.

18 It was completed, the premium is
19 represented as goodwill asset, the cost of the
20 goodwill asset is the utility's common equity,
21 which is in the capital structure. The asset,
22 however, is not being amortized, it's not in
23 rate base, but, nevertheless, the cost of
24 service for this utility is increased because of
25 the existence of the goodwill asset.

1 Q. Okay. And so the Company on the
2 short-term debt that is your adjustment number
3 one the Company's agreed to, there's been a
4 stipulation on that piece? You were first
5 talking with Commissioner -- with the Chairman,
6 you made two adjustments?

7 A. They did. Actually, at the true-up
8 date, they refinanced about \$170 million of
9 short-term debt with long-term debt and they did
10 include debt in their true-up capital
11 structures.

12 Q. Okay, so that one -- that adjustment's
13 been taken care of. So it really comes down to
14 this goodwill piece?

15 A. Yes.

16 Q. And I had it written down here
17 somewhere. So the capital structure without
18 removing the goodwill piece, you thought was
19 excessive?

20 A. Yes, because 57 percent of their direct
21 filing, 54 percent in their updated filing is an
22 equity ratio that exceeds what's necessary to
23 support their bond rating and it's also much
24 higher than the equity ratios typically allowed
25 LCD companies around the country.

1 Q. So that they adjusted the 54 percent --
2 there was -- I don't know if you were in the
3 room. I think it was the Company offered
4 true-up evidence of MGE back in 2014 where their
5 equity and debt ratio was roughly 54 percent
6 equity almost?

7 A. Yes.

8 Q. Was that excessive at that time?

9 A. I'm sure I took issue with it in the
10 gray (indicating) case leading up to it. You
11 know, I don't know what that filing was, if it
12 was a rate case filing or if it was simply a
13 reporting requirement and it really didn't
14 impact the development of rates, it was just
15 reporting earnings. And if that's the case,
16 then customers' rates weren't necessarily
17 adjusted to reflect that much common equity, but
18 their earnings, when they're reporting them to
19 the Commission, may have.

20 So I have to know a little bit more
21 about that report, but there is many filings
22 before the regulatory commission, and not all of
23 them are used to adjust rates to retail
24 customers.

25 COMMISSIONER RUPP: I think that's

1 all I have. Thank you.

2 THE WITNESS: Thank you.

3 JUDGE DIPPELL: Thank you.

4 Is there Cross-Examination based on
5 questions from the Bench from Staff?

6 MR. THOMPSON: No thank you, Judge.

7 JUDGE DIPPELL: Midwest Energy
8 Consumers?

9 MR. WOODSMALL: No questions.

10 JUDGE DIPPELL: Environmental
11 Defense Fund?

12 MS. KARAS: No questions, your
13 Honor.

14 JUDGE DIPPELL: Does Spire?

15 MR. PENDERGAST: Just few.

16 RE-CROSS-EXAMINATION BY MR. PENDERGAST:

17 **Q. You mentioned an Illinois legislation**
18 **that in some manner allocates equity to goodwill**
19 **and I think you mentioned formula rates.**

20 A. Yes.

21 **Q. Is that part of the formula rate**
22 **legislation that's, you know, been used to**
23 **regulate utilities in Illinois?**

24 A. The electric utilities, yes.

25 **Q. Okay. And, in fact, the formula rate**

1 legislation has a lot of different provisions to
2 it as far as how rates get adjusted and how ROE
3 gets set and how often it happens and that sort
4 of thing.

5 I'm just wondering would you recommend
6 a formula rate mechanism here in Missouri?

7 A. Well, no, but Ameren Missouri's gas
8 rates are set using the same kind of limits that
9 their electric side sets rates under. And the
10 gas rates are not set based on formula. They're
11 set based on traditional utility rate filings.
12 But, nevertheless, Ameren has entered into
13 agreements with the Staff and the industrial
14 groups in Missouri to not set rates with a
15 common equity ratio of greater than 50 percent,
16 again, recognizing that Ameren Illinois has a
17 lot of goodwill recorded on its balance sheet
18 and that causes the common equity ratio to go
19 up.

20 So it was enacted in law for the
21 electric formula rate process, but other
22 rate-making practices in Illinois result in some
23 utilities that have a lot of goodwill on their
24 balance sheets to make concessions with other
25 stakeholders in the rate case to use a capital

1 structure that the stakeholders find to be
2 reasonable for rate-making purposes.

3 **Q. Yeah, and I appreciate. My only**
4 **question was -- you mentioned, you know, the**
5 **goodwill feature of that legislation which also**
6 **has, you know, various formula rate features to**
7 **it.**

8 **And my only question was: You know,**
9 **taking the good with the bad, would you say**
10 **overall that that formula rate approach is**
11 **preferable and should be used in Missouri?**

12 **A. Quite honestly, no. I think it has**
13 **resulted in the utility kind of managing their**
14 **systems and increased their cost of service**
15 **under the formula rate. So I don't think it**
16 **gives stakeholders an adequate ability to really**
17 **test the reasonableness of the utility's cost**
18 **structure. So I do not recommend the formula**
19 **rate methodology be implemented here in**
20 **Missouri.**

21 **Q. And you agree that goodwill is created**
22 **as part of the completion of the final**
23 **transaction for an acquisition?**

24 **A. It's accounting mechanism.**

25 **Q. It's an accounting. And it's part of**

1 **that accounting for that transaction?**

2 A. To recognize the premium paid to the
3 book value or the fair value of the utility's
4 assets, yes.

5 **Q. And would you generally agree that**
6 **utilities are typically required under normal**
7 **regulatory and accounting policies to use the**
8 **net value -- net book value of their assets for**
9 **rate-making purposes?**

10 A. As a component of the rate-making
11 process, yes.

12 **Q. Is it also true that for income tax**
13 **purposes that this markup in assets,**
14 **specifically a 338(h)(10) election, is allowed**
15 **to show the true value of the acquired tangible**
16 **assets, if you know?**

17 A. I haven't looked at that specifically.

18 **Q. So you don't know if the tangible asset**
19 **gets stepped up in value?**

20 A. Well, I haven't looked at that
21 specifically for this transaction.

22 I do know in other transactions there's
23 been issue about whether or not it is a tax-free
24 transaction or not, and that has an impact as to
25 whether or not goodwill can actually be written

1 off for income tax purposes.

2 I assume that this was a tax-free
3 transaction when Laclede bought MGE because it's
4 my understanding they are not amortizing
5 goodwill against their income taxes. But I
6 haven't specifically looked at that.

7 **Q. But you're not sure?**

8 A. I do not know.

9 **Q. Okay. And, once again, I think in**
10 **answer to one of the Commissioner's questions,**
11 **you reconfirmed, if you will, that any goodwill,**
12 **any premium paid by Laclede Gas to acquire MGE**
13 **is not included in its rate base?**

14 A. Well, certain costs associated with it
15 are in their cost of service, but no part of the
16 goodwill asset is included in rate base.

17 **Q. Okay. And because it's not included in**
18 **rate base, customers are not paying a return on**
19 **that premium; is that correct?**

20 A. No, the operating income of the utility
21 is higher because the common equity supporting
22 the goodwill is in the proposed capital
23 structure.

24 **Q. Well... and as we established when this**
25 **acquisition took place, it was financed with an**

1 **equivalent amount of debt and equity; is that**
2 **correct?**

3 A. It did. I think Mr. Hevert's
4 testimony shows about \$450 million of debt for
5 about \$800 million of book value assets. So the
6 \$800 million of book value assets are in rate
7 base and the 450 million of the debt issued to
8 acquire those assets are included in the cap
9 structure.

10 **Q. So when it comes to the Company's**
11 **debt-to-equity ratio, the fact that you had an**
12 **equal amount of debt and an equal amount of**
13 **equity would tend to go ahead and flow into what**
14 **that capital structure is, would it not?**

15 A. It would for financial reporting. It
16 would not for measuring the utility's cost of
17 supporting the net book value of the asset
18 included in rate base.

19 That's the distinction and that's why
20 goodwill, which is only supported by common
21 equity, would distort the capital structure mix
22 for supporting rate-based investments if you
23 don't make an adjustment to the capital
24 structure.

25 **Q. And in paying that premium, that**

1 goodwill that was created, would an investor
2 look at what sort of benefits would be created
3 by the transaction?

4 A. Yeah, all investors look at the
5 expected cash flows after the transaction or
6 after the acquisition is made.

7 So just like a stock investor in Spire
8 right now would be willing to pay above book
9 value for that stock based on the expected
10 earnings in cash flow, Spire based on the
11 rate-making mechanisms allowed in each of its
12 regulatory jurisdictions -- that would include,
13 at least in Missouri, Spire's commitment not to
14 include any costs associated with that
15 acquisition premium or that goodwill asset. So
16 from an arms length transaction, investors are
17 willing to pay prices well above book value in
18 order to get a piece of the earnings that are
19 produced by a rate of return only on book value
20 assets.

21 Q. Okay. And just to look at it at a high
22 level, you are defining as a cost the failure,
23 is it, of Laclede Gas to reduce its normal
24 equity component that it's had, I think as you
25 admitted for quite sometime in the mid 50s, to

1 **47 percent, that's what you would define as a**
2 **cost?**

3 A. No, sir, what I would define as a cost
4 is what your actual capital structure mix is in
5 this rate case for supporting the assets
6 included in your rate base.

7 To the extent that common equity ratio
8 is lower now than it's been in the past doesn't
9 change the fact that that's how much common
10 equity is being used to support your rate base
11 investments in this case.

12 **Q. And I'm simply asking you, Mr. Gorman:**
13 **Is it your testimony that to avoid a cost to the**
14 **Company's customers, you need to go ahead and**
15 **use an equity component that is 70 or 80 basis**
16 **points lower than what Laclede has typically had**
17 **before any of these acquisitions occurred?**

18 A. Well, my answer isn't going to change
19 to that. I'm looking at what the capital cost
20 is that Laclede incurred to carry its rate base
21 in this investment.

22 I'm recommending you a fair return on
23 equity on the equity capital used to fund
24 investments in the utility infrastructure,
25 investments and you recover your debt cost on

1 the remaining components. So there is no
2 disallowance. Rather, it's simply an
3 improvement of identifying what your actual cost
4 of carrying your rate-based investments are.

5 **Q. What do you think the odds are we're**
6 **going to reach agreement on this point?**

7 A. (No response.)

8 (Pause in proceedings.)

9 **Q. And so you have 1.87 billion in your**
10 **capital structure -- billion, excuse me?**

11 A. (Reviewing document.)

12 Yes.

13 **Q. Okay. And do you know what Laclede's**
14 **actual rate base is?**

15 A. You know, this -- it was -- I believe
16 it's around 2 billion, but the difference is
17 because I simply took the Company's capital
18 structure and removed the common equity
19 supporting it.

20 If the Company synchronized its capital
21 structure to rate base, then this capital would
22 be less than the rate base, which means either
23 that there's more debt and equity in the
24 Company's balance sheet, which based on my
25 review of 10-K, that's not the case, or it would

1 be an indication that there's some short-term
2 debt being used to support investments in the
3 utility's rate base.

4 Q. So --

5 A. I haven't recommended the use of
6 short-term debt in developing an overall rate of
7 return in this case.

8 Q. Yeah, and we appreciate that. Thank
9 you. But Laclede has 2.1 billion in rate base
10 which are assets being used to serve customers?

11 A. That's right.

12 MR. PENDERGAST: Okay. Thank you.
13 No further questions.

14 JUDGE DIPPELL: Okay.

15 Mr. Gorman, I just wanted to get a
16 definition from you just to clarify the record.
17 When you referred to "10-K," you're referring to
18 an SEC filing?

19 THE WITNESS: Thank you, I am.
20 Security and Exchange Commission annual filing,
21 yes.

22 JUDGE DIPPELL: Okay. Thank you.

23 THE WITNESS: Thank you. I
24 apologize for that.

25 JUDGE DIPPELL: Oh, no, no, no

1 apology needed.

2 Is there Redirect? And we'll start
3 with OPC.

4 MR. SMITH: Yes. Thank you.

5 REDIRECT EXAMINATION BY MR. SMITH:

6 Q. Mr. Gorman, you were asked some
7 questions from a variety of parties on your
8 capital structure and how you arrived at it.

9 Do you have a copy of your Rebuttal
10 testimony?

11 A. I do.

12 Q. And would you turn to Schedule MPG-R-2?

13 A. (Witness so doing.)

14 I'm there.

15 Q. Would that be a good illustration of
16 how you arrived at your capital structure?

17 A. It is, yes. And that is the workpaper
18 used to develop it.

19 Q. Earlier Commissioner Rupp had asked you
20 some questions about the capital structure
21 relating to MGE. Do you recall those?

22 A. Yes.

23 Q. Would you agree that -- or I guess let
24 me ask this a different way.

25 Would the circumstances be different

1 comparing MGE to this case when you have MGE and
2 Laclede?

3 A. I'm sorry. Can you repeat that,
4 please?

5 Q. Yeah. Sure.

6 So you were discussing the capital
7 structure used for MGE with Commissioner Rupp.
8 Do you recall that?

9 A. Yes.

10 Q. And would you agree that the
11 circumstances for evaluating the capital
12 structure for -- in this case with updated
13 information and also including Laclede in
14 addition to MGE are different circumstances?

15 A. Well, they are different, sir. They're
16 different points in time, it's a different
17 company and there's different management
18 controlling the capital investment decisions and
19 I do understand that there's been some
20 infrastructure investments going on in each of
21 the jurisdictions. So the question is how were
22 they funding those infrastructure improvements?

23 All of that is encapsulated in what's
24 included in this rate file, and in looking at
25 that, the question then is: How much equity and

1 how much debt was used to invest in the utility
2 plant in this case? And I guess the -- another
3 question is whether or not short-term debt
4 should be included in the rate-making capital
5 structure.

6 So that is exactly the process I went
7 through to take the Company's recommended
8 capital structure and adjust it down to what I
9 think is an appropriate reflection of what the
10 Company's capital costs actually are for -- and
11 were relied on by the Company to invest in the
12 utility plant and equipment.

13 MR. SMITH: I have no further
14 questions.

15 JUDGE DIPPELL: MIEC?

16 MR. MILLS: Yes. Thank you.

17 REDIRECT EXAMINATION BY MR. MILLS:

18 **Q. Mr. Pendergast asked you a question**
19 **about when Laclede acquired MGE and asked**
20 **whether it was financed with roughly equal debt**
21 **and equity, and in your answer you emphasized**
22 **that the acquisition of the total company was**
23 **done with roughly debt and equity in equal**
24 **portions.**

25 Can you explain the emphasis on "total

1 **company"?**

2 A. Well, the acquisition funded both the
3 net book value of around \$800 million plus the
4 goodwill assets of about 210 million. That
5 total acquisition was roughly 50 percent debt
6 and 50 percent equity. But because utility debt
7 has to be serviced from investments that produce
8 cash flows, the amount of -- the portion of the
9 equity acquisition made by Laclede was the
10 \$800 million of net book value. So in
11 relationship to the utility debt to the net book
12 value, it was roughly 56 percent debt and about
13 44 percent equity or \$450 million of debt
14 relative to \$800 million of net book value and
15 about 44 million of equity relative to net book
16 value.

17 The additional \$210 million of the
18 acquisition price was premium to the net book
19 value, and that represented a transaction
20 between shareholders, not a transaction that
21 allowed the utility to secure capital from
22 investors and make investment in utility plant
23 and investment [sic]. Rather, it represented
24 capital where one utility shareholder bought the
25 stock of another utility shareholder.

1 **Q. Mr. Pendergast also asked you whether**
2 **or not you conducted an analysis of acquisitions**
3 **and synergies.**

4 **Was such -- is doing such an analysis**
5 **necessary for you to come to a supported**
6 **conclusion as to the appropriate capital**
7 **structure or return on equity in this case?**

8 A. It's not, but consistent with the
9 transaction that took place here, the Company
10 claimed that the acquisition would produce
11 significant synergies net of cost-to-achieve
12 synergies.

13 So it was more of a point of curiosity
14 to review their filing to see whether or not the
15 proposed transaction actually created the
16 benefits that they promised would be created at
17 the time they got authority to go forward with
18 the transaction and agreed not to include any
19 costs associated with the acquisition premium
20 and rates.

21 **Q. In response to question, I believe it**
22 **was a question from the Bench, you stated that**
23 **issuing debt to support goodwill would erode**
24 **credit standing. What do you mean by that?**

25 A. If the utility was issuing debt to

1 support the goodwill asset, then the level of
2 utility cash flows would not increase relative
3 to the amount of debt that was taken on because
4 goodwill doesn't produce cash flows.

5 On the other hand, by investing in
6 \$800 million of net book value plant assets for
7 MGE, those do produce cash flows and then can be
8 used to produce acquisition-related debt of
9 450 million.

10 To the extent the utility's total
11 amount of cash flows and the predictability of
12 those cash flows are weakened as a result of the
13 acquisition, then that would erode the credit
14 quality of the utility and we would see the
15 credit quality go down. So it would be
16 improvement for the utility to intentionally
17 finance a goodwill asset, one they know will not
18 produce cash flows because they committed not to
19 seek recovery of it from retail customers. So
20 it won't produce cash flows. If they financed
21 it with debt, that would have the effect of
22 reducing the cash available to fund debt on the
23 cash -- on the debt issued to fund the
24 transaction.

25 So I think it would be imprudent for

1 the Company to represent that they've funded the
2 goodwill asset with debt, although I think it is
3 prudent that the Company actually did fund the
4 acquisition of the net book value of MGE with
5 debt, because those do produce cash flows and I
6 do think that was a prudent financing decision.

7 **Q. Now, you were asked by Chairman Hall**
8 **about whether you proposed similar goodwill**
9 **adjustments in other cases, and you mentioned**
10 **several cases in which you had.**

11 **Have you ever been involved in a case**
12 **in which the utility had a percentage of**
13 **goodwill in its capital structure as significant**
14 **as the percentage in this case where you did not**
15 **propose an adjustment?**

16 A. No. No. I mean, the utility's common
17 equity is about a billion dollars in this case,
18 the goodwill asset's about 200 million. That's
19 20 percent of total outstanding common equity as
20 represented by goodwill asset.

21 If you compare that to Ameren Missouri,
22 it's also a de minimus percentage of the
23 acquisition adjustment or goodwill recorded on
24 their balance sheet. If you compare that to
25 Missouri American Water Company, they'd have

1 some goodwill asset, but that's because they're
2 acquiring some districts where their acquisition
3 actually benefits retail customers and there is
4 an opportunity for them to recover some of that
5 acquisition and premium from customers because
6 the transaction itself was so -- so much in
7 favor of customers that the Commission allowed
8 them to recover that acquisition adjustment and
9 rates.

10 The only other utility that had such a
11 large percentage of goodwill relative to total
12 common equity was Commonwealth Edison, and that
13 was created based on a sale of
14 nuclear-generating assets by Commonwealth Edison
15 when it converted from a vertically integrated
16 company down to only-wires company and then
17 there was a creation of emergent nuclear
18 generating company initially in the process
19 which ultimately turned into Exelon. But that's
20 the only other utility that had a very large
21 percentage of total common equity being
22 represented by the recording of a goodwill asset
23 that I'm aware of.

24 **Q. Okay. And I believe you testified in**
25 **that case the Illinois Commerce Commission**

1 **disallowed a portion of that goodwill asset that**
2 **was included in the capital structure?**

3 A. Well, they accepted a capital structure
4 adjustment, but the actual capital structure
5 adjustment resulted in a hypothetical capital
6 structure being used to set rates. The
7 Commission didn't exactly prescribe how it got
8 from the Company's requested capital structure
9 or my proposed capital structure to a capital
10 structure they found to be more reasonable, but
11 that capital structure that was found to be more
12 reasonable was closer to what I was recommending
13 than it was to what the Company was
14 recommending.

15 Q. And I believe you testified that in
16 recent cases you believed that you've identified
17 a trend in which the acquirer utilities agree
18 with stakeholders to not put goodwill into the
19 capital structure of the utility operated
20 company level; is that correct?

21 A. It is, yes.

22 Q. In this case could Spire Inc. have
23 recorded a goodwill on its books rather than on
24 Spire Missouri's books?

25 A. You know, I don't know specifically the

1 answer to that question, but I believe they
2 could have, you know, if Laclede Group could
3 have acquired MGE and then it could have merged
4 its subsidiaries together later.

5 But, frankly, I haven't looked into the
6 details of that and I don't know if there are
7 any restrictions on that.

8 **Q. Now, you answered some questions from**
9 **the Bench about the response of investors to the**
10 **Commission's awarding Ameren a nine and half**
11 **percent return on equity in the most recent**
12 **case, and I believe you said that the investment**
13 **community accepted that quite well.**

14 **So my question is: Did that award of**
15 **that level of return on equity have any**
16 **observable impact on the ability of Ameren to**
17 **provide safe and adequate service?**

18 A. Well, it certainly was a factor known
19 to the marketplace and we can see based on
20 verifiable market evidence that their stock
21 price is, I believe, the highest it's ever been.
22 Its dividend yield is probably as low as it's
23 ever been, at least as long as I've been
24 watching that company now. It's under 3
25 percent, well under 3 percent, which is very low

1 for an integrated utility company. Great Plains
2 Energy's price also is very high and its
3 dividend yield is right around 3 percent.
4 Again, that's very low relative to historical
5 standards. Both of them have very strong
6 investment grade bond ratings, they've been able
7 to issue debt at very low cost under reasonable
8 terms based on my review of their financial
9 records, and that is I believe observable market
10 evidence that the market believes that the
11 regulatory decisions made by this Commission
12 have been supportive of investors for those
13 utilities and the ability to come up with a
14 balanced outcome that is fair to both investors
15 and customers.

16 **Q. You are familiar, I believe, with the**
17 **stipulation and agreement in the acquisition**
18 **case?**

19 A. Laclede's acquisition of MGE? Yes.

20 **Q. Yes, that's the case I mean. And**
21 **Mr. Pendergast asked you some questions about**
22 **that, correct?**

23 A. Yes.

24 **Q. Is there any way to characterize the**
25 **inclusion of goodwill on capital structure other**

1 **than as an indirect impact of the acquisition**
2 **premium?**

3 A. No. I've represented MIEC -- and
4 certainly not in our mind because that's exactly
5 what we had expected, that there would be no
6 cost associated with goodwill that would be
7 included in the rate-making process, and that
8 includes not included in a rate base, not
9 amortizing it, but also excluding the common
10 equity from the rate-making capital structure.

11 **Q. So that including it in rate base and**
12 **amortizing, that would be a direct impact,**
13 **correct?**

14 A. Well, both are direct impacts.

15 **Q. Right.**

16 A. I mean, one's amortization cost and the
17 other is a carrying charge.

18 **Q. Right.**

19 A. So...

20 **Q. But the stipulation didn't stop when it**
21 **said "direct cost." It added the phrase**
22 **"indirect cost" as well, did it not?**

23 A. It did, yes.

24 **Q. Moving on to some questions that Mr.**
25 **Pendergast asked you about requirements for, I**

1 **believe, tracking tangible assets, is goodwill a**
2 **tangible asset?**

3 A. I believe it is recorded under plant
4 and service. I believe the accounting is to
5 recognize it as a tangible asset.

6 **Q. Now, finally, with respect to the**
7 **acquisition premium itself, did the ratepayers**
8 **of Laclede or MGE have any choice in the level**
9 **of acquisition premium that Laclede paid for**
10 **MGE?**

11 A. No, they weren't part of the
12 management's negotiating on the acquisition
13 price.

14 The only leverage customers had was in
15 negotiating the settlement where Laclede agreed
16 not to seek recovery of any of those transaction
17 costs for those goodwill-related costs in the
18 rate-making process.

19 **Q. And if Laclede had not represented**
20 **to -- that it would not include either directly**
21 **or indirectly any costs of that acquisition**
22 **premium, do you think the parties and the**
23 **Commission itself would have looked more closely**
24 **at the level of that acquisition premium in the**
25 **acquisition case?**

1 A. Well, I can tell you that where MIEC
2 was headed was to lay out what we meant by "cost
3 associated with goodwill" up until we reached
4 the settlement with the Company.

5 So had we filed testimony, that would
6 have broken that out explicitly like that. But
7 the settlement, we thought, captured what
8 everybody had agreed to, and that is no costs
9 associated with goodwill would be included in
10 the rate-making process.

11 MR. MILLS: Thank you. That's all
12 the questions I have.

13 JUDGE DIPPELL: Thank you.

14 Mr. Gorman, I believe that ends your
15 testimony, and you may step down and you are --
16 let me see, was that your only issue?

17 THE WITNESS: Yes, it is.

18 JUDGE DIPPELL: Okay, you may be
19 excused.

20 THE WITNESS: Thank you.

21 (Witness excused at 4:49 p.m.)

22 JUDGE DIPPELL: All right. Well,
23 that conveniently puts us at the end of the day,
24 so we will go ahead and break for the day.

25 We can begin again at 8:30 in the

1 morning and move a little quicker through some
2 issues. So we will start with the issues that
3 we didn't get this time with the -- now, did I
4 have somebody that was only available on the
5 12th or was it just the 13th?

6 MR. WOODSMALL: 13th.

7 JUDGE DIPPELL: Just the 13th.

8 Okay.

9 Then we will pick up where we left off
10 in the morning with opening statements on that
11 issue. We can adjourn.

12 (Whereupon, the hearing was recessed
13 at 4:50 p.m. CST.)

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C E R T I F I C A T E

STATE OF MISSOURI)
) ss.
COUNTY OF ST. LOUIS)

I, Deborah Habian, Certified
Shorthand Reporter with the firm of Alaris
Litigation Services, do hereby certify that I was
personally present at the proceedings had in the
above-entitled cause at the time and place set
forth in the caption sheet thereof; that I then
and there took down in Stenotype the proceedings
had; and that the foregoing is a full, true and
correct transcript of such Stenotype notes so made
at such time and place.

Given at my office in the City of
St. Louis, County of St. Louis, State of Missouri.


DEBORAH HABIAN, CSR, RMR, CRR, CBC
Notary Public
CSR No. 084-02432

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