Exhibit No.:	
Issue:	Financing Authority
Witness:	Mark D. Waltermire
Type of Exhibit:	Rebuttal Testimony
Sponsoring Party:	Laclede Gas Company
Case No.:	GF-2009-0450
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LACLEDE GAS COMPANY

GF-2009-0450

REBUTTAL TESTIMONY

OF

MARK D. WALTERMIRE

REBUTTAL TESTIMONY OF MARK D. WALTERMIRE

Q. Please state your name and business address.

A. My name is Mark D. Waltermire, and my business address is 720 Olive Street, St. Louis, Missouri 63101.

Q. By whom are you employed and in what capacity?

A. I am employed by Laclede Gas Company in the position of Senior Vice President and Chief Financial Officer.

Q. Please describe your qualifications and work experience.

A. I was elected to my current position in 2007. As Senior Vice President and Chief Financial Officer, I am responsible for a number of functions at the Company, including financial reporting, accounting, treasury, billing, compliance with Sarbanes-Oxley and Securities and Exchange Commission requirements, and information technology activities. Since joining Laclede in 1990, I have held a number of other positions including Manager of Rate and Financial Planning, Director of Internal Audit, Assistant Vice President, Planning and Vice President, Operations and Marketing. Prior to joining Laclede, I held positions as Senior Accountant for Deloitte & Touche, Division Controller for St. Joe Minerals Corporation, and Vice President and Treasurer for Newhard, Cook & Co., Incorporated, a regional securities broker/dealer. I hold a B.S. Degree in Accounting from the University of Illinois and am a Certified Public Accountant.

Q. What is the purpose of your rebuttal testimony in this case?

A. The purpose of my testimony is to respond to the direct testimony filed by Staff witness Zephania Marevangepo in this case. Specifically, I will explain why the rote, formulaic approach recommended by Mr. Marevangepo for determining how much long-term debt Laclede should be authorized to issue is not appropriate. I will also address why the justifications given by Mr. Marevangepo for applying that formula in this case, and for proposing other restrictions on the ability of Laclede to issue other kinds of financing instruments, are equally invalid.

Q. What is your understanding of the formula being used by Mr. Marevangepo to determine the level of long-term debt that he believes Laclede should be authorized to issue?

A. Mr. Marevangepo has essentially proposed that Laclede's authorization be limited to only that amount of long-term debt that is necessary to support: (a) the Company's projected capital expenditures over the next three years; plus (b) any scheduled repayment of currently outstanding long-term debt; minus (c) projected funds from operations over the next three years after the payment of dividends. However, Mr. Marevangepo has also proposed to round the resulting figure up to $100 million, so that an actual debt offering might be of a more marketable size.

Q. Why is such a formula inappropriate?

A. At the outset, I believe such a formula is inappropriate because it assumes that there is a need for additional limitations on how the Company exercises its existing financing authority. There is absolutely nothing in Laclede's previous use of the financing authority granted by the Commission, however, that would warrant such an action. To the contrary, throughout its history and, more recently, throughout the extreme and almost unprecedented disruptions which occurred in the credit markets, Laclede has been an exceptional steward of its financial resources. Our ability to maintain an "A" credit rating, the conservative and efficient way in which we have issued long-term debt in the past, and the degree to which we have maintained a healthy capital structure are all illustrative of the Company's success in this regard. Given these considerations, I do not see any basis for the suggestion that additional limitations, above those safeguards previously approved by the Commission, are at all necessary.

Q Why else is the formula inappropriate in your view?

A. By placing severe limitations on the amount of long-term debt that Laclede can issue, such an approach would also significantly erode the agility with which the Company can access the capital markets that are so vital to the Company's ability to carry out its public utility obligations. It would also fundamentally alter the current, and I believe far more appropriate, regulatory practice of allowing utilities to determine the specific timing and mix of their financings – subject to a subsequent review of the prudence of such decisions – and replace it with a system where the Commission would effectively make such decisions, or at least approve them in advance. Company witness Lynn Rawlings has already addressed these considerations in some detail in her direct testimony. As the Chief Financial Officer for the Company, however, I feel compelled to emphasize just how important full and timely access to all facets of the capital markets is for a company like Laclede to acquire the additional funds it requires to make investments in utility assets and why the approach recommended by Mr. Marevangepo would seriously erode such access in the future.

Q. Why is full and timely access to the capital markets particularly important for a company like Laclede?

A. Like many other utilities, Laclede is a capital intensive business that must routinely invest over $50 million each year to expand, maintain and replace the thousands of miles of pipes needed to distribute gas to our customers. As a gas distribution utility, Laclede must also have adequate financing available to purchase, store and transport the gas supplies required to furnish service and to carry customer balances.

Q. What implications does this kind of financial profile have for the Company?

A. It means that the resources necessary to finance our utility operations cannot be satisfied solely through internally-generated funds, but instead must also come from investors, bondholders, banks and other external sources of money. These include the equity and bond investments generally used to finance long-lived assets such as mains, service lines, and regulators and the other capital components of our utility infrastructure, as well as the commercial paper, bank lines of credit, and other debt instruments generally used to finance shorter-term purchases of gas, hedging instruments, and other operational cash requirements. In some cases, these financial resources must be attracted and retained for literally decades to pay for utility plant and other regulatory assets, the recovery of which may be spread over twenty, thirty or even more years, depending on the asset at issue. In other situations, funds are needed for shorter periods of time but in far greater amounts. The hundreds of millions of dollars in short-term debt that Laclede incurs to finance gas purchases months in advance of when it receives customer payment for the related services is one example.

Q. Has the Company's need for these financial resources increased over the years?

A. Yes, as Ms. Rawlings explained, they have increased significantly in recent years.

Q. Why is the formula used by Mr. Marevangepo for determining his cap on long-term issuances inadequate to meet this need?

A. Because it arbitrarily and unnecessarily reduces the amount of long-term debt that the Company may use to address these needs. Laclede understands the point that there should be a relationship between the amount of long-term debt it carries on its books and the value of its utility assets. In fact, that is precisely why Laclede has previously agreed to the Staff-proposed and Commission-approved safeguard that its total long-term debt issuances not exceed the value of its regulated rate base. The main problem with Mr. Marevangepo's formula is that it severs this relationship by arbitrarily ignoring the value of the assets on the Company's books and by arbitrarily allocating to <u>future</u> capital expenditures all funds from <u>current</u> operations.

Q. In what way does Mr. Marevangepo's formula ignore the value of the assets on the Company's books?

A. Actually, it understates the value of these assets in two ways. First, Mr. Marevangepo's formula only recognizes assets obtained through future capital expenditures, presumably on the theory that they are the only kind of assets that require longer-term financing. In fact, the Company carries tens of millions of dollars of Commission-authorized regulatory assets on its books that, while not the product of a traditional capital expenditure, require the same kind of longer-term financing.

Q. Can you provide some examples of these kinds of assets?

A. Surely. Among others, the Company currently has regulatory assets associated with its pension plan, other post-retirement benefits ("OPEBs") such as retiree medical costs, expenditures associated with its energy efficiency programs, costs incurred to comply with changes in the Commission's Cold Weather Rule, and deferrals associated with certain safety-related investments. In each of these instances, gains were recognized sooner or costs were spread over a longer period of time so that rates could be kept lower in the near-term. Sometimes this result was accomplished by reducing rates to reflect the value of market-related gains in pension plan assets (even though such gains could not be taken out of the pension fund) while in others it occurred by deferring until future rate cases actual expenditures that were being made by the Company for Commission-approved programs (e.g. safety-related and energy efficiency expenditures). The point is that each of these ratemaking policies created a regulatory asset that, while not physical in nature, requires financing for a period longer than one year, just as physical assets do. Despite the fact that these kinds of assets now account for a significant portion of the Company's rate base, however, Staff's formula completely ignores them.

Q. How else does the formula used by Mr. Marevangepo understate the value of the Company's assets?

A. By focusing solely on future capital expenditures, Mr. Marevangepo's formula also fails to recognize all of the capital expenditures that the Company has made in the past in excess of its long-term issuances. Obviously, this will also result in a mismatch between the amount of long-term debt issued by the Company and the value of its regulated assets.

Q. Is such an exclusion consistent with the statutes governing the Commission's approval of utility financings?

A. I am not an attorney and am not in a position to render a legal opinion. I would note, however, that the same statute cited by Mr. Marevangepo at page 7 of his direct testimony, namely Section 393.200, specifically authorizes a utility to issue long-term debt to pay for "unreimbursed expenditures" for capital items made in the five-year period immediately prior to a financing request.

Q. Do the Commission's rules also recognize that repayment of unreimbursed expenditures is a legitimate purpose for which long-term debt may be issued?

A. Yes. In fact, the Commission's rules specifically require that a utility include a five-year historical capital expenditure schedule in its financing application, presumably to facilitate this kind of result. *See* 4 CSR 240-3.220(1)(G).

Q. Did the Company file such a schedule as part of its application in this case?

A. Yes, it did. As shown by Exhibit 3, page 3, to our Verified Application, the Company had approximately $279 million in unreimbursed expenditures for property additions over the five-year period preceding the filing of its application.

Q. Does the Staff's formula for determining the amount of long-term debt authorization it is recommending make any allowance for reimbursing these previous capital expenditures?

A. No, none whatsoever. In fact, by limiting Laclede to *projected* capital expenditures only, plus repayment of retiring debt, Staff's formula effectively precludes the Company from issuing long-term debt for this purpose even though such a purpose is explicitly permitted by the statute.

Q. You also indicated that Staff's formula understates the amount of long-term debt Laclede should be authorized to issue because it subtracts projected "funds from operations" from the Company's projected capital expenditures. Why is this inappropriate?

A. Staff's formula simply assumes that all projected funds from operations (except that portion used to pay dividends) should be used to finance future capital expenditures, which therefore reduces Staff's recommended long-term debt authorization level. I concur with Staff that a portion of our funds from operations should be used to provide shareholders with an opportunity to obtain a return on and to be reinvested in *all* utility assets. Given that, I do not see why it is appropriate to assume that all remaining funds should be used *exclusively* to finance *future* capital expenditures versus other cash outlays that the Company must make to provide utility service. It is doubly inappropriate, however, for the Staff to reflect the earnings and depreciation associated with these prior capital expenditures in its formula while simultaneously ignoring the expenditures themselves, including those that have not been reimbursed. Such inconsistent treatment seems to have no purpose or rationale other than to artificially reduce the amount of long-term debt that the Company should be authorized to issue. In addition, Staff proposes to give this authorization on the basis of projections alone – projected capital expenditures and projected funds from operations – without any allowance for the virtual certainty that reality will differ from these projections.

Q. What effect does the use of funds from operations to reduce future long-term debt authorizations have on the Company's short-term debt levels?

A. Staff's proposal to apply 100% of the net funds from operation entirely to future long-term financing needs will hamper the Company's ability to pay down its short-term debt. In the same testimony that he expresses a concern that Laclede's short-term debt levels are too high, Mr. Marevangepo urges adoption of a contradictory proposal that will serve to increase short-term debt in the future.

Q. Staff's formula also appears to assume that the Company's projected capital expenditures should be funded with 35% equity, consistent with the 65% to 35% debt-to-equity ratio previously approved by the Commission in GM-2001-0342. Is this appropriate?

A. No. The requirement that Laclede maintain a 65%/35% debt-to-equity ratio was just that – an overall capital structure requirement that could not be exceeded by Laclede. As Ms.

Rawlings has previously testified, Laclede has fully complied with this safeguard, as evidenced by the fact that we have maintained a debt ratio of less than 50%; a circumstance that again reflects our prudent use of debt. Staff's formula simply ignores these facts, however, by inappropriately applying the ratio to incremental rather than overall financings – a result that, as a matter of simple math, will lock in a debt-to-equity ratio that is much lower than the 65%/35% ratio previously approved by the Commission. This is a Staff position that again results in an artificial reduction in the amount of long-term debt that the Company should be authorized to issue.

Q. Does the historical safeguard approved by the Commission for determining how much long-term debt Laclede should be allowed to issue suffer from any of these deficiencies?

A. No. In contrast to Staff's formula, the current requirement that long-term debt issuances not exceed the value of the Company's regulated rate base maintains the flexibility necessary to ensure that the Company will continue to have the kind of robust access to the capital markets needed to meet its public utility obligations. Consistent with the financing purposes contemplated by the statute, it also provides enough headroom to issue long-term debt in amounts sufficient to cover those unreimbursed capital expenditures previously made by the Company, should that be advisable. At the same time, this safeguard, as well as the other previously-approved ones discussed by Ms. Rawlings in her direct testimony, ensures than any long-term debt issuances made by the Company will not detrimentally impact the Company's financial condition or disturb the proper match between such issuances and the utility assets they support. For all of these reasons, I believe the current safeguards are far superior to the formula proposed by Staff in this proceeding.

Q. Do the current safeguards also address the concerns expressed by Mr. Marevangepo at pages 3-6 of his direct testimony that long-term debt not be issued to finance operational needs?

A. Yes. While I disagree with Mr. Marevangepo's comment that working capital does not contribute to growth, these safeguards nevertheless ensure that the Company can never issue more long-term debt than what can be supported by the Company's regulated assets. That, in turn, ensures that such debt will not be used to fund shorter term operational expenditures. However, one cannot ignore the extra demands on the Company's cash resources generated by certain kinds of operational expenditures, such as hedging costs, that can impose financial obligations on the Company for periods in excess of the one year statutory dividing line between what is considered short-term versus long-term debt. While the safeguards mentioned above guarantee that long-term debt won't be issued to pay such operating costs, ignoring these obligations and their contribution to the need for greater, rather than less, financing flexibility is a mistake.

Q. Does this same consideration also apply to the limitations that Staff has recommended regarding the Company's authority to enter into capital leases and issue preferred stock?

A. Yes. Although Mr. Marevangepo has repeated in his direct testimony Staff's recommendation to limit the use of capital leases and prohibit the issuance of preferred stock outright, he really offers no explanation as to why such financing options are inappropriate. Accordingly, I can only note at this point that Laclede's proposal to count the value of any such financings toward the long-term debt limitation safeguards currently imposed by the Commission completely addresses any concerns that could conceivably relate to the use of these alternative financing vehicles over the next three years. In fact, since capital leases and preferred stock can be viable alternatives to satisfying the same longer-term financing needs, there is really no meaningful basis for treating these financing options differently so long as they are all subject to the same safeguards.

Q. At page 4 of his direct testimony, Mr. Marevangepo expresses a concern that the Company's seasonal short-term debt levels have increased over the past three years and have not been eliminated or reduced to zero in each of these years as has "usually" been the case. Does that concern have any bearing on the level of long-term debt that the Company should be authorized to issue?

A. I do not believe Mr. Marevangepo has presented any facts to support the contention that this recent experience with short-term debt levels should be a cause for alarm or even concern. In fact, these relatively higher short-term debt levels over the past several years are exactly what one would have expected to see given the extraordinary impact that higher natural gas prices and hedging costs had on the Company's cash requirements over this same period of time. Given the degree to which these impacts have been quantified for the Staff on numerous occasions, any insinuation that there is some mystery surrounding the reasons for this increase in short-term debt levels is completely unwarranted. To the contrary, to the extent it has any relevance to the issues under consideration in this proceeding, this experience with short-term debt levels simply provides another data point supporting the Company's position that maintaining financing flexibility and agility is more important today than it has ever been. In any event, in the time since the Company's original application was filed in this case on June 30, 2009, the Company has continued to make significant progress in reducing its short-term debt. Short-term debt at our fiscal year end of September 30, 2009, was $130 million, down from $304 million one year earlier. In addition, our short-term debt level for February of this year reached an intra-month low of $64 million, compared to $268 million at the same date last year. In short, whatever one wishes to make of the relevance of Laclede's short-term debt levels in recent years, the fact remains that we are currently on track to reduce our outstanding short-term debt to more traditional levels on a seasonal basis.

Q. At page 8 of his direct testimony, Mr. Marevangepo also mentions the need for more regulatory scrutiny of Laclede's debt financing because of the growth in the Company's non-regulated operations, including those of Laclede Energy Resources. Do you agree with this statement?

A. As a general proposition, I can understand why scrutiny of affiliate transactions is necessary, and I thought that's precisely why the Commission has affiliate transactions rules: to protect utility customers when such transactions are conducted. What I don't understand is why Mr. Marevangepo would raise such a concern at this point in this proceeding. As Mr. Marevangepo acknowledges, he did not even mention this consideration in his initial Memorandum and Recommendation in this proceeding, something I would have expected if this were truly a substantive concern. Moreover, Staff has been repeatedly advised that Laclede Gas does not lend money to its affiliates, but rather has been an occasional borrower of money from its parent company. I would also note that the very first condition placed on the authority granted by the Commission in Laclede's previous financing cases, and in Staff's Recommendation in this case, expressly prohibits the Company from using the proceeds of any authorized financing "for any purpose other than for the exclusive benefit of Laclede Gas Company's regulated operations…" This strict condition, which Laclede has consistently agreed to and complied with for many years, certainly provides the necessary regulatory protection, particularly since it applies whether the non-regulated operations are growing, shrinking, or standing still. Given these considerations, I do not believe that the generalized concern that has been raised by Mr. Marevangepo at the last moment should be given any weight, particularly since it is completely unaccompanied by any facts showing that there is an actual problem that needs to be addressed.

Q. Does this conclude your rebuttal testimony?

A. Yes, it does.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Laclede Gas Company's Verified Application for Authority to Issue and Sell First Mortgage Bonds, Unsecured Debt and Preferred Stock, in Connection with a Universal Shelf Registration Statement, to Issue Common Stock and Receive Capital Contributions, to Issue and Accept Private Placement Securities, and to Enter Into Capital Leases, all in a Total Amount Not to Exceed $600 Million	))))))))	Case No. GF-2009-0450

<u>AFFIDAVIT</u>

STATE OF MISSOURI)
) SS.
CITY OF ST. LOUIS)

Mark D. Waltermire, of lawful age, being first duly sworn, deposes and states:

1. My name is Mark D. Waltermire. My business address is 720 Olive Street, St. Louis, Missouri 63101; and I am Senior Vice President and Chief Financial Officer of Laclede Gas Company.

2. Attached hereto and made a part hereof for all purposes is my rebuttal testimony, on behalf of Laclede Gas Company.

3. I hereby swear and affirm that my answers contained in the attached testimony to the questions therein propounded are true and correct to the best of my knowledge and belief.

Mark D. Waltermire

Mark D. Waltermire

Subscribed and sworn to before me this 12 day of March, 2010.

JOANNE E. ALLEN
Notary Public - Notary Seal
STATE OF MISSOURI
St. Louis County
My Commission Expires: Oct. 5, 2013
Commission # 09878750

Joanne E Allen

Notary Public