

MEMORANDUM

TO: Missouri Public Service Commission
Official Case File Case No. GF-2018-0249

FROM: David Murray, CFA, Utility Regulatory Manager, Financial Analysis Department

/s/ David Murray, CFA 8/8/2018 /s/ Jeffrey A. Keevil 8/8/2018
Project Coordinator / Date Staff Counsel's Office / Date

SUBJECT: Staff Recommendation concerning the Application of Spire Missouri Inc. ("Spire Missouri," "Company," or "Applicant") for Approval of Financing

DATE: August 8, 2018

1. (a) **Type of Issues:** Registered or Private Placement Debt, Common Stock, and Capital Leases.

(b) **Amount:** Up to \$500,000,000 of all securities (except for current Operating Leases with a term of 12 months or more which are required to be recharacterized as Capital Leases due to implementation of the Accounting Standards Update issued February 26, 2016 by the Financial Accounting Standards Board).

(c) **Rate:** Unknown and not applicable in terms of stock.

(d) **Other Provisions:** Further terms and provisions including provisions for prepayment and redemption will be determined at the time of issuance.
2. **Proposed Date of Transactions:** Anytime during the requested period of financing authority through September 30, 2021.
3. (a) **Statement of Purpose of the Issuances:** The proceeds from the securities will be used for the following purposes: 1) to discharge or redeem previously issued bonds; 2) to finance the purchase, acquisition and construction of additional properties and facilities, as well as improvements to the Company's existing plant; 3) to improve or maintain service; 4) to discharge or lawfully refund all or a portion of the Company's outstanding short-term debt; 5) to reimburse moneys actually expended from income; and/or 6) to provide the financial resources required to meet the Company's other public utility obligations.

(b) **From a financial perspective, does Staff deem this Statement of Purpose of the Issue reasonable?**

Yes, with some exceptions and conditions.

**** Denotes Confidential Information ****

APPENDIX A

4. **Copies of executed instruments defining terms of the proposed securities:**

No instruments have been executed and no general terms or conditions were described other than potential for private or registered (public) debt securities.

5. **Certified copy of resolution of the directors of applicant, or other legal documents authorizing the issuance of the securities reviewed:**

Yes

6. **Pro-forma Balance Sheet and Income Statement reviewed:**

Yes

7. **Capital expenditure schedule reviewed:**

Yes

8. **Journal entries required to be filed by Spire Missouri to allow for the Fee Schedule to be applied:**

Unknown until securities are issued.

9. **Recommendation of the Staff:**

Authorize \$500 million of all securities (other than current Operating Leases with a term of 12 months or more which are required to be recharacterized as Capital Leases due to implementation of the Accounting Standards Update issued February 26, 2016 by the Financial Accounting Standards Board, which will not count against the Financing Authority [see Comments and Recommended Conditions]).

COMMENTS:

Spire Missouri is a public utility engaged in distributing and transporting natural gas to customers in both the eastern and western portions of the State of Missouri. Spire Missouri serves customers in the City of St. Louis and ten (10) counties in eastern Missouri through its Spire East operating unit. Spire Missouri serves customers in the City of Kansas City and thirty (30) counties in western Missouri through its Spire West operating unit. Spire Missouri is a gas corporation subject to the jurisdiction of the Missouri Public Service Commission. Spire Missouri is a wholly-owned subsidiary of Spire Inc., which owns other companies.

Spire Missouri filed this Application pursuant to Sections 393.180 and 393.200 RSMo (the Application should also have referenced Section 393.190), and Commission Rules 4 CSR 240-2.060 and 3.220. The Application requests that the Commission grant Spire Missouri the

authority to issue registered securities (presumably first mortgage bonds, unsecured debt and preferred stock), issue private placement debt, and issue common stock all in a total amount not to exceed \$500 million.

Spire Missouri also requests that the authority granted by the Commission apply to an accounting change taking effect in 2019 that will have the impact of reclassifying certain existing operating leases to capital leases. Spire Missouri has stated that this accounting change will not result in any incremental change to its financing needs and, accordingly, does not expect that any incremental financing authority is needed to accommodate the change. However, if incremental financing authority is needed due to the accounting change, Spire Missouri requests that it be deemed as having the requisite financing authority to accommodate any change in the amount of capital leases it carries resulting from the new accounting requirement, and that any such amounts not be counted against its \$500 million financing authority. Staff is not opposed to this request.

Spire Missouri lists the following potential uses of the proceeds that would be raised pursuant the requested authority: (1) to discharge or redeem previously issued bonds; (2) to finance the purchase, acquisition and construction of additional properties and facilities, as well as improvements to the Company's existing plant; (3) to improve or maintain service; (4) to discharge or lawfully refund all or a portion of the Company's outstanding short-term debt; (5) to reimburse moneys actually expended from income; and/or (6) to provide the financial resources required to meet the Company's other public utility obligations. These potential uses are generally contemplated under Section 393.200(1) RSMo, even if some of the listed uses are no longer practical under modern corporate financing practices.

Spire Missouri's Application requests the Commission provide it authority to issue various securities in an amount of up to \$500 million through September 30, 2021. In order to evaluate the reasonableness of Spire Missouri's request, Staff issued data requests to request financial data as it pertains to the period in which Spire Missouri is requesting the Commission grant it financing authority. Staff requested Spire Missouri provide projected financial statements for this period, any information Spire Missouri provided to or received from rating agencies during its most recent interaction with rating agencies, and the pro forma impact of the proposed financings on Spire Missouri's projected credit metrics over the period of the requested financing authority. Staff requested this information in order to assess the reasonableness and necessity of Spire Missouri's request and the potential impact of requested debt issuances on credit quality.

For purposes of estimating potential capital needs, it is common corporate financing practice to estimate the difference between the amount of funds the company expects to receive from its operations and the amount of funds the company expects to use in its operations (inclusive of capital expenditures and dividend payments). To the extent that there is a projected deficiency in the amount of funds the company has available for reinvestment in its operations, the company usually incurs short-term debt to initially fund these deficiencies. To the extent short-term debt balances reach sustained, higher levels due to investment in long-lived assets, it is financially prudent to issue long-term financings to reduce the amount of short-term debt outstanding. This allows for adequate capacity to access short-term capital markets to maintain sufficient liquidity. Consequently, Staff issued its data requests in this case to determine not only Spire Missouri's projected capital deficiency, but also how the planned financings requested in the Application may impact Spire Missouri's credit quality by analyzing certain key credit metrics, to which rating agencies give significant consideration.

According to Spire Missouri's projected cash flow statements ** _____ . ** Being that this is the scenario Spire Missouri presented to rating agencies in June 2018 and the rating agencies have not published reports expressing concerns about such planned debt issuances, Staff is not particularly concerned about Spire Missouri ** _____. ** Staff's concerns in past Spire Missouri finance applications was that their requested financing authority was far in excess of anticipations shared with rating agencies, which would mean something unexpected and possibly financially detrimental had occurred, which Staff and the Commission should review.

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Due to the significant disparity between Spire and Spire Missouri's capital structures in the most recent rate cases, GR-2017-0215 and GR-2017-0216, Staff analyzed Spire's and Spire Missouri's projected capital structures to determine if Spire and Spire Missouri's capital structures will become more similar. In Staff's opinion, Spire's decision to **

_____. ** Because each company's financial risk is interrelated, it is important to evaluate the planned financial management of each company to ensure Spire Missouri's low business-risk assets are appropriated a fair amount of debt capacity, which may reduce its cost of capital. ** _____

_____ 1 _____

_____ **

Because Spire Missouri is requesting a broad financing authority for the next three years, the Application does not provide details as to the anticipated terms of the debt it plans to issue over the period of the authority. In fact, although the financial projections indicate ** _____

_____, ** this would be at the Company's discretion. Because the Company cannot provide more defined terms of anticipated debt issuances over the period of the Authority, Staff believes it would be prudent to condition the Authority to only securities that are consistent with the types of securities the Company has issued in the past, specifically as it relates to debt securities. For example, ** _____

_____. ** If the Company plans to issue debt other than senior secured debt, then it should notify the Commission 90 days in advance of its plan to issue such securities and explain the reason it believes it is prudent.

Staff recommends the Commission grant Spire Missouri the full amount of its requested financing authority, subject to the following conditions:

1. That the Company be authorized to issue registered securities (first mortgage bonds, unsecured debt and preferred stock), issue common stock, and issue private placement debt in an aggregate amount not to exceed \$500 million at any time, or from time to time, through September 30, 2021, provided that the Company shall not be authorized to use any portion of the \$500 million for any purpose other than for the exclusive benefit of Spire Missouri's regulated operations, as such purposes are specified in Section 393.200. However, if the Company plans to issue anything other than senior secured debt

¹ Measured as total debt (long-term debt and short-term debt) as a percentage of total capital (common equity + total debt).

(registered or privately-placed), it shall file notification with the Commission ninety (90) days in advance of doing so.

2. That Spire Missouri is authorized to accommodate any change in the amount of capital leases it carries resulting from the accounting standards update adopted by FASB on February 16, 2016. Any such amount shall not count against the amount of the financing authority granted herein by the Commission.
3. That the total amount of the long-term debt, capital leases, and preferred stock issued and outstanding under such authorization shall not, at any time during the period covered by this authorization, exceed the lesser of the value of Spire Missouri's rate base or 65 percent of its total capitalization, as such conditions are defined in Case Nos. GM-2001-342 and GF-2007-0220.
4. That the current Commission Authority under Case No. GF-2015-0181 shall be superseded by the Authority granted in Case No. GF-2018-0249.
5. That the interest rate for any debt issuance covered by the Application shall not be greater than a rate that is consistent with similar securities of comparable credit quality and maturities issued by other issuers.
6. That, if and when individual debt securities are issued under this Application, the Company shall submit a verified report to the Commission's Budget & Fiscal Services Department documenting such issuance, the use of any associated proceeds and the applicability and measure of fees under Section 386.300.2.
7. That the Company shall file with the Commission within ten (10) days of the issuance of any financing authorized pursuant to a Commission order in this proceeding a report including the amount issued, date of issuance, interest rate (initial rate if variable), maturity date, redemption schedules or special terms, if any, use of proceeds, estimated expenses, and loan or indenture agreement concerning each issuance. In addition, the Company shall also provide the analysis, to include but not be limited to indicative pricing information developed, performed to determine that the terms for the securities issued were consistent with market requirements at the time.
8. That the Company shall submit to Staff and The Office of the Public Counsel any information concerning communications with credit rating agencies concerning individual debt securities issued under this Application.
9. That the Company shall file with the Commission any credit rating agency reports issued on the Company, the Company's debt issuances, or on Spire Inc.
10. That nothing in the Commission's order shall be considered a finding by the Commission of the value of these transactions for rate making purposes, and that the Commission


reserves the right to consider the rate making treatment to be afforded these financing transactions and their results in cost of capital, in any later proceeding.

11. In seeking a renewal of the authority granted in this case, Spire Missouri and Staff shall operate under the general time frames set forth for financing cases in the 2004 case management roundtable project.

The Staff respectfully requests that this matter be placed on the Commission's Agenda as soon as possible.

In the Matter of Spire Missouri Inc. d/b/a)
 Spire's Verified Application to Renew Its) **Case No. GF-2018-0249**
 Financing Authority)

STATE OF MISSOURI)
COUNTY OF COLE) SS


David Murray, CFA

Dianna L. Vaughn
Notary Public

