

Exhibit No. \_\_\_\_\_  
Issue: Cost of Capital (Debt)  
Witness: Michael E. Thaman, Sr.  
Type of Exhibit: Direct Testimony  
Sponsoring Party: Indian Hills  
Case No.: WR-2017-0259  
Date: October 13, 2017

**Missouri Public Service Commission**

**Direct Testimony**

**of**

**Michael E. Thaman, Sr.**

**On Behalf of**

**Indian Hills Utility Operating Company, Inc.**

**October 13, 2017**

IH Exhibit No. 13  
Date 11-27-17 Reporter KF  
File No. WR-2017-0259



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DIRECT TESTIMONY OF  
MICHAEL E. THAMAN, SR.

1 WITNESS INTRODUCTION

2 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

3 A. My name is Michael E. Thaman, Sr. My business address is Warson Capital  
4 Partners, LLC, 7733 Forsyth Boulevard, Suite 1450, St. Louis, MO 63105.

5 Q. PLEASE DESCRIBE YOUR FORMAL EDUCATION.

6 A. I received a Bachelor of Science with a major in Accounting from the University  
7 of Missouri – Columbia in 1971.

8 Q. PLEASE DESCRIBE YOUR PROFESSIONAL EXPERIENCE.

9 A. My professional experience includes the following:

10 a. 1971 – 1981: Practice as a Certified Public Accountant with the St. Louis  
11 office of KPMG, an international accounting firm.

12 b. 1981 – 1991: Executive Vice President and Chief Financial Officer of  
13 Landmark Bancshares Corporation, a \$2.5 billion banking organization  
14 based in St. Louis, now part of Regions Bank.

15 c. 1992 – 1994: CEO of NationsMart Corporation, a consumer services  
16 company which completed an IPO in 1993.

17 d. 1994 – present: Co-Founder and CEO of Warson Capital Partners, LLC, an  
18 investment banking and private equity firm based in St. Louis providing debt  
19 and equity capital to emerging growth companies in a wide range of  
20 industries.

1 Q. WHAT EXPERIENCE DO YOU HAVE IN REGARD TO THE FINANCING OF  
2 BUSINESSES?

3 A. My experience with respect to financing businesses began in the mid-1970s as a  
4 member of management at the international accounting firm KPMG working with  
5 clients who were having difficulty in arranging financing for a variety of reasons  
6 including distressed or "turnaround" situations. In that capacity, I pursued  
7 financing from both traditional and nontraditional sources. As CFO of Landmark  
8 Bancshares Corporation for eleven years, I (i) lead the process of raising more  
9 than \$100 million of private and public debt and equity financing to fuel growth of  
10 the company, ultimately listing the company on the New York Stock Exchange;  
11 and (ii) served on our community banks' executive loan committees participating  
12 in the analysis and approval process for loan proposals from clients in a variety  
13 of industries including a few public utilities. I often worked with clients whose  
14 loan proposals were rejected, usually for lack of traditional credit worthiness, to  
15 identify and pursue alternative sources of financing. As co-founder and CEO of  
16 Warson Capital Partners for 23 years, I have represented more than 100 client  
17 companies in raising debt and/or equity financing in both local and national  
18 markets. Many of these clients have been start-up situations, early-stage  
19 emerging growth companies, and in some cases "turnaround" situations, most  
20 requiring nontraditional financing.

21

1 **PURPOSE**

2 **Q. WHAT IS THE PURPOSE OF YOUR DIRECT TESTIMONY?**

3 A. I will discuss the general non-availability of traditional financing for water utilities  
4 in the condition of Indian Hills Utility Operating Company, Inc. (Indian Hills), and  
5 the reasons therefore, as well as the reasonableness of the debt rate being  
6 charged to Indian Hills.

7 **COST OF CAPITAL (DEBT)**

8 **Q. WHAT DOCUMENTS HAVE YOU REVIEWED IN PREPARATION FOR YOUR**  
9 **TESTIMONY?**

10 A. I have reviewed the Direct Testimony of Josiah Cox; "Appendix F HC to  
11 Application to PSC for transfer of assets BS at Acquisition", a part of the original  
12 Indian Hills asset transfer and financing case; historical financial statements of  
13 Indian Hills as of and for the year ended December 31, 2016, and as of and for  
14 the nine months ended September 30, 2017; "Partial Disposition Agreement and  
15 Request for Evidentiary Hearing Case No. WR-2017-0259"; "Report of Customer  
16 Service and Business Operations Review – Consumer and Management  
17 Analysis Unit Small Company Rate Increase Request Case No. WR-2017-0259";  
18 "Recommended Rate of Return for Indian Hills Utility Operating Company, Inc. as  
19 of March 31, 2017 Case No. WR-2017-0259" and related schedules; a file  
20 created by Indian Hills entitled "Indian Hills Credit Risk Profile"; "Small Utility  
21 Return on Equity/Rate of Return Methodology" prepared by the Financial  
22 Analysis Department of the Utility Services Division of the Missouri Public

1 Service Commission dated September 2010; and Missouri Office of the Public  
2 Counsel "Small Utility Rate Case Tutorial" prepared by Ted Robertson, CPA.

3 **Q. WHAT DO YOU UNDERSTAND IS INDIAN HILLS' ACTUAL COST OF DEBT?**

4 A. Fourteen percent (14%).

5 **Q. DOES THAT DEBT COST SURPRISE YOU?**

6 A. No it does not surprise me, considering the true risk profile of Indian Hills and the  
7 resulting nature of the debt.

8 **Q. PLEASE EXPLAIN.**

9 A. In my opinion, the risk profile of small utilities in the condition of Indian Hills,  
10 particularly with respect to financial position, results of operations, out-of-  
11 compliance status, regulatory control of utility rates and related issues, and the  
12 potential for unknown contingent liabilities ("Distressed Utilities"), is such that  
13 traditional bank financing is not available. Any lender to Distressed Utilities  
14 would be entering into a financing arrangement with significant high-risk  
15 characteristics, completely outside of traditional bank capital markets. There is  
16 no bond rating, stated, adjusted or otherwise, that could apply to this risk profile.  
17 As a result, very few sources of financing are available.

18 **Q. WHAT TYPES FINANCING MIGHT BE AVAILABLE TO INDIAN HILLS?**

19 A. Financing for distressed public utilities such as Indian Hills is very difficult to  
20 source. The few sources that may be available would be specialized  
21 infrastructure venture investors, high-net-worth private investors, opportunistic  
22 specialty-situation financing firms, and similar high-risk investors who would  
23 likely: (i) be familiar with small utilities and particularly Distressed Utilities, the

1 risks that may be associated therewith, the cost and the time required to  
2 eliminate or mitigate such risks, the management team and its ability to address  
3 those risks; and (ii) be willing to take the risk of a loan with significant high-risk  
4 characteristics in exchange for a commensurate rate of interest. Such  
5 commensurate rate of interest would be determined by such sources of financing  
6 based on their own assessment of risk, a process that is highly subjective  
7 because of the many unknowns, financial and otherwise, associated with  
8 Distressed Utilities. Given that there exists no established market for this type of  
9 financing, Distressed Utilities are fortunate when they do locate a source of  
10 financing, but find themselves with very little negotiating position.

11 **Q. WHAT IS THE INTEREST RATE FOR THESE TYPES OF FINANCING?**

12 A. Based on my experience, lenders to companies with risk profiles similar to that of  
13 Indian Hills could expect returns in the range of fifteen (15%) to twenty-one  
14 percent (21%) for such loans.

15 **Q. DO YOU HAVE AN OPINION AS TO THE REASONABLENESS OF THE 14%  
16 INTEREST RATE ASSOCIATED WITH INDIAN HILLS'S FINANCING?**

17 A. Yes. Based on the risk profile of Indian Hills and the very few alternatives  
18 available for financing, I believe the fourteen percent (14%) interest rate  
19 associated with Indian Hills's financing is reasonable.

20 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

21 A. Yes.