

**STATE OF ILLINOIS**  
**ILLINOIS COMMERCE COMMISSION**

THE PEOPLES GAS LIGHT :  
AND COKE COMPANY :  
 : No. 11-\_\_\_\_  
Proposed General Increase :  
In Rates For Gas Service :

Direct Testimony of

**LISA J. GAST**

Manager

Financial Planning and Analysis  
Integrys Business Support, LLC

On Behalf of

The Peoples Gas Light and Coke Company

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1 **I. INTRODUCTION AND BACKGROUND**

2 **A. Witness Introduction**

3 Q. Please state your name and business address.

4 A. My name is Lisa J. Gast. My business address is Integrys Energy Group, Inc.  
5 (“Integrys”), 700 North Adams Street, P.O. Box 19001, Green Bay, WI 54307-9001.

6 Q. By whom are you employed and what is your current position?

7 A. My current position is Manager Financial Planning and Analysis for Integrys Business  
8 Support, LLC (“IBS”), which is a wholly-owned subsidiary of Integrys.

9 Q. For whom are you providing testimony?

10 A. I am providing testimony for The Peoples Gas Light and Coke Company (“Peoples Gas”  
11 or the “Company”), which is a wholly-owned indirect subsidiary of Integrys.

12 **B. Purpose of Testimony**

13 Q. What is the purpose of your direct testimony?

14 A. The purpose of my direct testimony is to present and support the Company’s forecasted  
15 cost of capital, or its overall rate of return on its rate base, which is comprised of  
16 estimated cost of common equity, embedded cost of long-term debt and proposed capital  
17 structure, all for the 2012 test year. The return on equity component of the cost of capital  
18 is presented by Peoples Gas witness Mr. Paul Moul in his direct testimony (PGL Ex. 3.0).  
19 I provide the capital structure and long-term debt components.

20 **C. Summary of Conclusions**

21 Q. Please summarize your conclusions regarding the appropriate capital structure, return on  
22 common equity and embedded cost of long-term debt for the Company for test year 2012.

23 A. As shown in PGL Ex. 2.1, the Company estimates a cost of capital and rate of return on  
24 rate base for the 2012 test year of 8.49%, which reflects a capital structure of 56%  
25 common equity and 44% long-term debt, a cost of equity of 11.25%, and an embedded  
26 cost of long-term debt of 4.97%.

27 **D. Itemized Attachments to Direct Testimony**

28 Q. Are you sponsoring any exhibits?

29 A. Yes, I am sponsoring the following exhibits:

<u>Exhibit No.</u>	<u>Corresponding 83 Ill. Admin. Code Part 285 Schedule</u>
PGL Ex. 2.1	D-1 Cost of Capital Summary
PGL Ex. 2.2	D-3 Embedded Cost of Long-Term Debt
PGL Ex. 2.3	D-7 Comparative Financial Data
PGL Ex. 2.4	D-8 Security Quality Ratings

30

31 **E. Background and Experience**

32 Q. Please describe your educational background and business experience.

33 A. I graduated from the University of Wisconsin – Green Bay with a Bachelor’s Degree in  
34 Accounting. I have also received a Masters Degree in Business Administration from the  
35 University of Wisconsin – Oshkosh. My professional designations are Certified Public  
36 Accountant and Certified Treasury Professional. I joined the Treasury Department of  
37 Wisconsin Public Service Corporation (“WPSC”), a wholly-owned subsidiary of  
38 Integrys, in April 2001.

39 Q. What are your responsibilities in your present position?

40 A. As Manager Financial Planning and Analysis, I direct the financial analysis and  
41 forecasting, for Integrys and its affiliates, including Peoples Gas. I am also responsible

42 for the capital structure and the cost of debt forecasts for each of Integrys' six regulated  
43 electric and natural gas utilities.

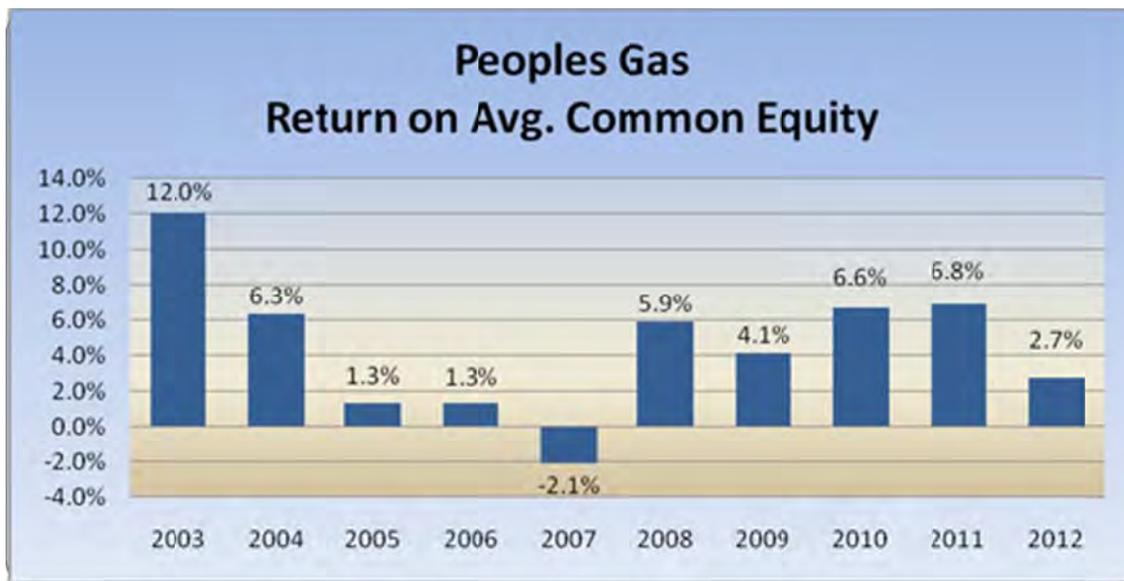
44 **II. AUTHORIZED RATE OF RETURN**

45 Q. Why is it important that the Company be allowed the opportunity to earn its test year cost  
46 of capital through the setting of the authorized return on rate base?

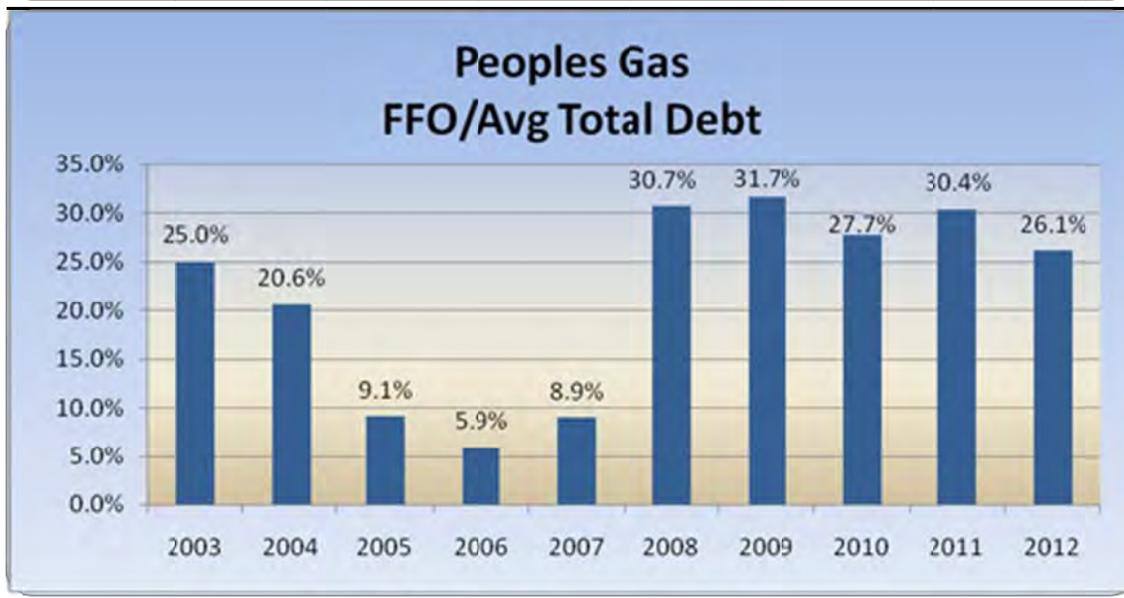
47 A. This is important because the Company's obligation to provide safe, adequate and  
48 reliable service to its customers at just and reasonable rates requires that it maintain its  
49 financial integrity and its ability to readily access the capital markets on reasonable terms  
50 and conditions. A strong capital structure, like that proposed by the Company, is  
51 consistent with the capital structures authorized in its last two rate cases, as well as  
52 current market expectations. A strong capital structure is important in maintaining the  
53 Company's investment grade credit ratings, and protecting the Company and its  
54 customers from financial shocks. A strong capital structure is especially important  
55 during times of financial market instability and economic uncertainty. Likewise, it is  
56 important that the Company be allowed an opportunity to earn a fair and reasonable rate  
57 of return on its investment that is consistent with the return expected by investors on  
58 investments of comparable risk. This in turn necessitates, among other things, that the  
59 allowed return on rate base be set equal to the utility's actual cost of capital in the test  
60 year. If the Company is not permitted an opportunity to earn its full cost of capital, its  
61 financial integrity and ability to raise capital on reasonable terms will be at risk, which  
62 will ultimately threaten its ability to meet its service obligations.

63 Q. How have the Company's returns on equity and its key credit ratios changed in recent  
64 years, and how will they be impacted absent the requested rate relief?

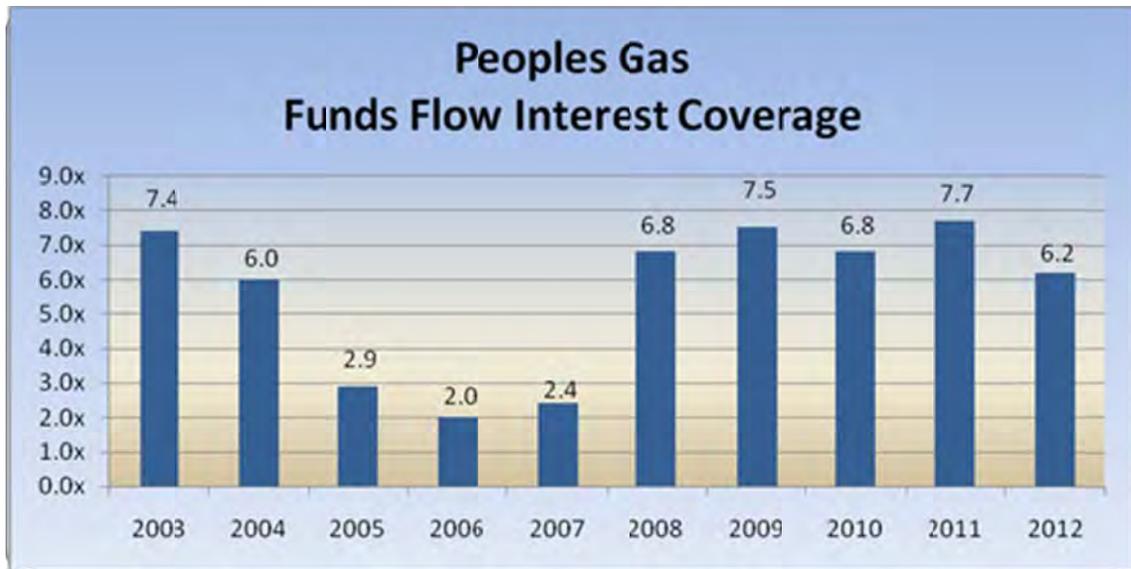
65 A. As shown in Peoples Gas Ex. 2.3 and summarized in the charts below, although the  
 66 Company's equity returns and key credit metrics have improved as a result of the 2008  
 67 and 2010 rate increases, these increases were not adequate to fully restore the Company's  
 68 required returns and credit metrics. Indeed, absent rate relief, the credit metrics  
 69 associated with the 2012 test year are insufficient to maintain the Company's current  
 70 credit ratings or its ability to raise capital on reasonable terms.



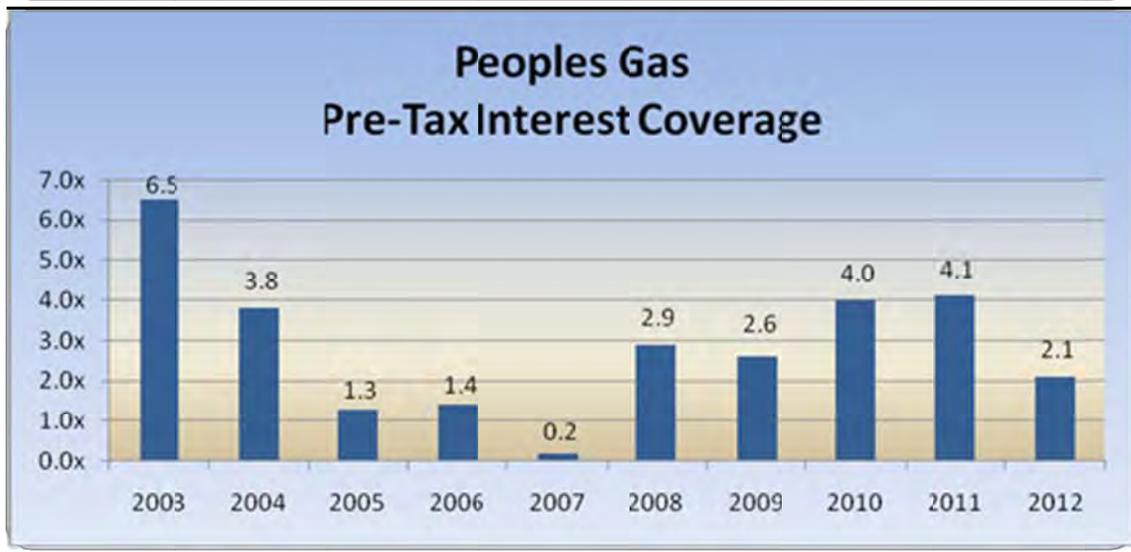
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75 **III. COMMON EQUITY RATIO**

76 Q. Please describe the corporate structure of Peoples Gas and its relationship to Integrys.

77 A. Peoples Gas is an Illinois corporation and a wholly-owned indirect subsidiary of Integrys,  
 78 a Wisconsin corporation and a public utility holding company. Shares of Integrys trade  
 79 on the New York Stock Exchange under the symbol "TEG." Peoples Gas has no existing  
 80 authority to sell common equity to any other entity, and has no plans to seek such  
 81 authority.

82 Q. Does Peoples Gas issue debt independently of Integrys?

83 A. Yes. Peoples Gas issues first mortgage bonds to public and private investors  
84 independently of Integrys for the purpose of funding long-term investment in rate base.  
85 The long-term debt of Peoples Gas is owned entirely by public and private investors;  
86 none is held by Integrys. Peoples Gas also issues commercial paper to private investors  
87 to meet its short-term seasonal cash requirements.

88 Q. Does Peoples Gas also borrow from its affiliates?

89 A. Yes, the Commission has granted approval for Peoples Gas to borrow funds on a short-  
90 term basis from its corporate parent, and from its affiliate, North Shore Gas Company.

91 **IV. CAPITAL STRUCTURE OBJECTIVES**

92 Q. What capital structure does Peoples Gas propose for the purposes of its 2012 revenue  
93 requirement?

94 A. Peoples Gas proposes a capital structure consisting of 56% common equity and 44%  
95 long-term debt.

96 Q. Is this proposed capital structure reasonable and appropriate for Peoples Gas?

97 A. Yes. As a public utility with an obligation to serve, Peoples Gas must have ready access  
98 to the capital markets at reasonable rates when required under all types of market  
99 conditions. A strong capital structure helps to provide for such access by allowing the  
100 Company to maintain strong credit ratings on its debt. As shown in PGL Ex. 2.4, Peoples  
101 Gas currently maintains reasonably strong credit ratings, with ratings on its senior  
102 secured debt of A- from Standard & Poors and A1 from Moody's.

103 A strong capital structure also helps to insulate the Company from “event-driven”  
104 financial shocks. This is particularly important during periods of financial market  
105 volatility and provides flexibility when gas prices fluctuate to extreme levels. A strong  
106 capital structure also reduces the Company’s costs by reducing its cost of debt as well as  
107 the cost of providing credit in various forms to counter-parties. For all of these reasons,  
108 the proposed capital structure is reasonable and appropriate for Peoples Gas.

109 Q. How does the Company’s proposed capital structure for the 2012 test year compare to its  
110 currently authorized capital structure?

111 A. It is the same. In its January 21, 2010 order in Docket Nos. 09-0166 and 09-0167 (cons.)  
112 (at p. 93), the Commission authorized a capital structure comprised of 56% common  
113 equity and 44% long-term debt. In its February 5, 2008 Order in Docket Nos. 07-0241  
114 and 07-0242 (cons.) (at p. 73), the Commission also authorized the same capital structure  
115 for the Company in its 2008 test year rate case.

116 Q. How does the proposed capital structure for the 2012 test year compare to the Company’s  
117 actual capital structure?

118 A. The proposed capital structure approximates the Company’s actual November 2010 year-  
119 to-date capital structure, as well as the average capital structure maintained by the  
120 Company over the past several years. As shown in PGL Ex. 2.3, Peoples Gas’ November  
121 2010 year-to-date capital structure was 56.6% common equity and 43.5% long-term debt.  
122 The November 2010 year-to-date 13-month average capital structure was 56.4% common  
123 equity and 43.6% long-term debt. Over the five year period 2005-2009, the Company’s  
124 year-end capital structure averaged 55.8% common equity and 44.2% long-term debt.

125 Q. Is the proposed capital structure reasonable when compared with the proxy group of  
126 companies (“the Gas Group”) used by Company witness Mr. Moul to develop his return  
127 on equity recommendation?

128 A. Yes, as discussed in Mr. Moul’s testimony and shown in his exhibits, the Company’s  
129 proposed common equity ratio is similar to the 2009 average for the Gas Group and is  
130 somewhat less than the Value Line forecasted average common equity ratio of more than  
131 58% for those companies.

132 **V. COST OF COMMON EQUITY**

133 Q. What is the Company’s forecasted cost of common equity for 2012?

134 A. As estimated by Mr. Moul, the Company’s forecasted cost of common equity in 2012 is  
135 11.25%.

136 **VI. EMBEDDED COST OF LONG-TERM DEBT**

137 Q. What is the embedded cost of long-term debt included in the proposed test year cost of  
138 capital for Peoples Gas?

139 A. The embedded cost of long-term debt included in the proposed test year cost of capital is  
140 4.97%, as shown in PGL Ex. 2.2.

141 Q. How has the Company’s pro forma embedded cost of long-term debt changed since its  
142 last rate order?

143 A. The pro forma embedded cost of long-term debt reflects changes in the Company’s  
144 outstanding indebtedness, both actual and planned, since its 2010 rate order in Docket  
145 Nos. 09-0166/09-0167 (cons.) as summarized below.

		Forecasted	Effective	Maturity		Rate in	Rate
		Rate	Date	Date	Amount	2010	Change
(1)	Series OO	-			51,000,000	1.00	(1.00)
(2)	Series UU	4.630			75,000,000	7.43	(2.80)
(3)	Series VV	2.125	8/18/2010	3/1/2030	50,000,000	4.75	(2.63)
(4)	Series WW	2.625	10/5/2010	2/1/2033	50,000,000	3.75	(1.13)
(1)	New - 10 Year	4.450	6/1/2011	6/1/2021	100,000,000		
	New - 10 Year	5.900	3/1/2012	3/1/2022	50,000,000		
(1)	Proceeds from June 2011 fixed rate issuance used to replace variable rate Series OO in October 2011						
(2)	2010 test year forecast was for a \$50 million issuance						
(3)	Replaced Series HH						
(4)	Replaced Series LL						

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147 Q. Does this complete your direct testimony?

148 A. Yes.