MICHAEL E. THAMAN, SR.
REBUTTAL TESTIMONY

Exhibit No. ___________
Issue: Cost of Capital (Debt)
Witness: Michael E. Thaman, Sr.
Type of Exhibit: Rebuttal Testimony
Sponsoring Party: Indian Hills
Case No.: WR-2017-0259
Date: October 27, 2017

Missouri Public Service Commission

Rebuttal Testimony

of

Michael E. Thaman, Sr.

On Behalf of

Indian Hills Utility Operating Company, Inc.

October 27, 2017

AFFIDAVIT

STATE OF Missouri)
) ss
COUNTY OF St Louis)

I, Michael E. Thaman, Sr., state that the answers to the questions posed in the attached Direct Testimony are true to the best of my knowledge, information and belief.

Subscribed and sworn to before me this 26th day of October, 2017.

Notary Public

My Commission Expires:

Kathleen M. Follmer
State of Missouri - St. Louis County
Notary Public Commission #12533887
My Commission Expires 4/18/2020

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MICHAEL E. THAMAN, SR.

INTRODUCTION AND PURPOSE

Q. Please state your name and business address.

A. My name is Michael E. Thaman, Sr. My business address is 7733 Forsyth Boulevard, Suite 1450, St. Louis, Missouri 63105.

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

A. I am a Partner of Warson Capital Partners, LLC.

Q. Are you the same Michael E. Thaman, Sr. that provided direct testimony in this proceeding?

A. Yes.

Q. What is the purpose of your rebuttal testimony?

A. The purpose of my rebuttal testimony is to respond to the Direct Testimony of Messrs. Michael P. Gorman and Greg R. Meyer, witnesses for the Missouri Office of the Public Counsel ("OPC") concerning the financing of Indian Hills Utility Operating Company, Inc. ("Indian Hills" or the "Company"), the cost of such financing, bank debt applications, and potential corporate financial activities within a multi-subsidiary corporate entity.

II. RESPONSE TO MICHAEL P. GORMAN

Q. What is your professional assessment of Mr. Gorman's cost of debt recommendation in this case?

A. Mr. Gorman presents a textbook, hypothetical analysis through which he arrives at an imputed cost of debt, which he states, without support, has been shown to comply with certain objectives of prudent utility management, minimization of cost of service to ratepayers, and preservation of a utility's financial integrity and access to capital. On the surface, this hypothetical analysis and the words surrounding it sound good from a textbook perspective, and perhaps may apply to large utilities such as those that qualify for bond ratings from Standard & Poor's ("S&P") and Moody's. However, with respect to this case regarding Indian Hills, the underlying assumptions to Mr. Gorman's hypothetical analysis bear no resemblance to the reality of securing financing for a very small, distressed and unrated utility such as Indian Hills. Therefore, such hypothetical analysis and the resulting conclusions are invalid with respect to evaluation of the reasonableness of Indian Hills actual cost of debt, and should be dismissed by the Commission.

Q. Please describe the assumptions to Mr. Gorman's hypothetical analysis that you consider to be invalid.

A. Mr. Gorman states that he investigated the current cost of debt for a below investment grade utility company. The term "below investment grade" indicates that the utility does have a bond rating from one or both of S&P and Moody's. It is not possible for a very small and distressed utility such as Indian Hills to achieve a rating of any kind from either of these institutions. Therefore, the comparison of the current cost of debt for a below investment grade utility company to the cost of debt for a small and distressed utility such as Indian Hills is invalid. Mr. Gorman goes on to identify Dayton Power and Light ("DPL"), a subsidiary of AES Corp., as the below investment grade utility he chose for recent debt issuance costs to be applied in his hypothetical analysis for Indian Hills' cost of debt. The table below provides a comparison of DPL and Indian Hills.

Comparison of DPL and Indian Hills

Measure	**DPL[1]**	**Indian Hills[2]**
Service Provided	Electric	Water
Customers	519,000	715
Service Area	6,000 mi^2	6.5 mi^2
Assets	$1,935,316,257	$2,225,816
Revenues	$1,346,554,101	$73,120
2016 Actual Capital Structure	67.73% debt, 32.26% equity	87.46% debt, 12.53% equity
Debt Issue Size	$200,000,000[3]	$1,450,000
Debt Issue Coupon Rate	6.75%[4]	14.00%
Moody's bond rating	Baa3[5]	NONE

DPL is a subsidiary of AES Corp., a New York Stock Exchange ("NYSE") listed Fortune 200 global power company. AES provides energy to 17 countries through its portfolio of distribution businesses as well as thermal and renewable

1 Dayton Power and Light Company 2016 FERC Form 1.
2 Indian Hills' 2016 Annual Report filed with the Missouri PSC.
3 From Schedule MPG-3.
4 *Ibid.*
5 From Moody's on-line report for DPL at October 25, 2017.

generation facilities. AES has a workforce of 19,000 people, and reported revenues of $14 billion and total assets of $36 billion as of and for the year ended December 31, 2016.[6] Clearly, DPL and Indian Hills are in no way comparable, as DPL is several times larger than Indian Hills with 519,000 customers, operates in a different industry than Indian Hills, has secured a rating from both S&P and Moody's, and is owned by a multi-billion-dollar worldwide NYSE-listed company. Therefore, the comparison of the current cost of debt for DPL to the cost of debt for a small, distressed and unrated utility such as Indian Hills is invalid. Based on these facts, Mr. Gorman's hypothetical analysis and the resulting conclusions are invalid with respect to evaluation of the reasonableness of Indian Hills actual cost of debt, and should be dismissed by the Commission.

II. RESPONSE TO GREG R. MEYER

Q Is the corporate structure of First Round CSWR, LLC ("CSWR") and its subsidiaries customary for companies such as this?

A. Yes.

Q. In your experience, is it common for multi-unit companies such as CSWR to transfer equity capital between the holding company and its subsidiaries and between subsidiaries as described in Mr. Greg R. Meyer's Direct Testimony?

A. Yes. Having served as CFO of a NYSE-listed multi-unit holding company, and President and CEO of a NASDAQ-listed multi-unit company, I have experienced transfers such as those described in Mr. Meyer's Direct Testimony in the normal course of business to provide for unit needs. Such transfers do not impact the

[6] AES Corp website at October 25, 2017.

measurement of a unit's operating performance. Of course, it is the Company's responsibility to maintain full and accurate records of such transfer activity as part of its regular accounting system to provide for external review such as monitoring by the Office of the Public Counsel.

Q. Describe your experience in the banking industry and in particular your experience in reviewing and responding to loan applications.

A. From May 1981 through December 1991, I served as Executive Vice President and Chief Financial Officer of Landmark Banks, a $2.5 billion bank now part of Regions Bank. In such position, my responsibilities included serving on the Bank's executive committee and executive loan committees which regularly reviewed the larger loan applications proposed by our loan officers for approval. During this time, I participated in the review of thousands of loan applications.

Q. Describe your experience as an investment banker in working with banks for financing on behalf of your clients.

A. As a Founder and Partner of Warson Capital Partners, LLC for 23 years, I have served many clients in financing and/or refinancing their companies, arranging both debt and equity funding from many sources including traditional commercial banks.

Q. Describe your view of the typical process of a bank in receiving and evaluating loan requests.

A. As a very high-level description, bank commercial lenders ("Lenders") receive requests for loans from prospective borrowers generally beginning with a meeting and discussion of a company's financing needs and a proposed structure for such financing. If it appears to a Lender that the prospective borrower's proposal meets the bank's criteria or can be refined to meet the bank's criteria, the Lender will typically work with the prospective borrower requesting the documents and information needed to develop an application package to meet the Lender's requirements in presenting a loan request to the bank's loan committees. Lenders are very careful to take a loan request to committee only if the Lender truly believes such requested loan will be approved to avoid wasting time for the borrower, the Lender and the committee. Lenders generally know early in the process whether or not a loan proposal meets the bank's criteria and is worth the time of pursuit, and they generally are quick to inform prospective borrowers when they believe the proposal is not a fit for their bank. Such rejection is typically communicated in a face-to-face meeting, a telephone call or an email.

Q. Do you believe the Company's actions with respect to applications for financing and the form of rejections received as described in Mr. Meyer's Direct Testimony are customary in today's banking environment?

A. Yes, based on the information provided in Mr. Meyer's Direct Testimony, the bank's rejections are very typical responses.

Q. Have your reviewed the Indian Hills bank loan application?

A. Yes.

Q. What is your opinion as a former banker and current investment banker of the quality and thoroughness of the Indian Hills bank loan application?

A. Upon my review, I found the Indian Hills bank loan application to be of high quality and very thorough such that, should a Lender be interested in considering a loan to Indian Hills and proceed with a review, I believe such Lender would be very impressed and pleased with the form, content, and thoroughness of the Indian Hills bank loan application.

Q. Do you believe the Company should be able to obtain financing on more favorable terms than the terms contained in the Company's existing loan and security agreement?

A. Based on my experience and ongoing activity in the debt markets, I know of no source of financing for the Company on terms more favorable than its existing arrangement. As stated in my direct testimony, financing for distressed public utilities such as Indian Hills is very difficult to source. The few sources that may be available would be specialized infrastructure venture investors, high-net-worth private investors, opportunistic specialty-situation financing firms, and similar high-risk investors who would likely: (i) be familiar with small utilities and particularly Distressed Utilities, the risks that may be associated therewith, the cost and the time required to eliminate or mitigate such risks, the management team and its ability to address those risks; and (ii) be willing to take the risk of a loan with significant high-risk characteristics in exchange for a commensurate rate of interest. Such commensurate rate of interest would be determined by such sources of financing based on their own assessment of risk, a process that is highly subjective because of the many unknowns, financial and otherwise, associated with Distressed Utilities. Given that there exists no established market for this type of financing, Distressed Utilities are fortunate when they do locate a source of financing, but find themselves with very little negotiating position. Lenders to companies with risk profiles similar to that of Indian Hills could expect returns in the range of fifteen (15%) to twenty-one percent (21%) for such loans.

Q. Do you have experience with large institutional lenders?

A. Yes, I have worked with large institutional lenders including money center banks and insurance companies.

Q. In your experience, what is the minimum size loan package required for large institutional lenders?

A. Generally $25 million to $50 million.

Q. Why do these institutions establish minimums such as you describe?

A. Financial institutional lenders understand that the acquisitions costs generally incurred to complete a loan often will be about the same for smaller loans as for the larger loans. Through cost/benefit analyses, these institutional lenders have determined that such minimums are required to provide adequate returns from their lending business. Further, institutional lenders often expect bond ratings for their loans, and achievement of such ratings is unlikely for transactions below the established thresholds.

Q. Have new utilities received terms different from those included in the Company's loan agreement?

A. Yes. I am aware that Elm Hills Utility Operating Company, Inc. was recently approved by the Commission, unopposed by the OPC, for a financing that included half of the prepayment penalty seen in previous CSWR loans. I also have seen a very recent debt term sheet for a new set of utility acquisitions for Confluence Rivers Utility Operating Company, Inc. This new term sheet provides a small interest rate reduction.

Q. Based on your overall experience and assessment of the market for small distressed utilities, has the Company made good progress on loan terms and conditions?

A. Yes, my observation is that the Company has made good progress with respect to loan terms and conditions.

Q. Do you believe a large refinancing of all of the utilities owned and operated by CSWR providing lower overall financing costs is possible in the future?

A. Yes, assuming mitigation of the risk factors and an aggregation of utility debt to an amount that meets the institutional minimums.

Q. Have you reviewed the potential debt re-finance scenarios generated by Indian Hills?

A. Yes.

Q. Do they reflect a reasonable potential method to lower debt costs?

A. Yes.

Q. Do you review business plans in your investment banking business?

A. Yes. During my 23 years in the investment banking business, I have reviewed hundreds of business plans covering most industries.

Q. Is it customary for the business plan of an early-stage company to include reference to a possible exit partner?

A. Yes. Many early-stage business plans include reference to possible exit partners as one form of exit to provide a reasonable possibility of protection for debt and equity investors. Particularly with high-risk companies such as regulated distressed utilities, an investor's acceptance of such high risk is often premised on an understanding of reasonable exit alternatives that can generally be expected, although never assured, to provide at a minimum for return of capital.

Q. Do you have any other comments?

A. Yes. Mr. Meyer's Direct Testimony appears to be circular. He appears to attempt to impugn the operations of a company that is operating at a cash loss in order to provide safe and reliable service, and then states that a utility that is operating at a cash loss should have access to lower-costing financing. These positions are incongruous, and from the perspective of a lender, the resulting regulatory uncertainty demonstrated in this testimony only serves to increase the risk profile of small distressed utilities such as Indian Hills.

Q. Does this conclude your Rebuttal Testimony?

A. Yes, it does.