BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

DOCKET NO. E-7, SUB 1243
DOCKET NO. E-2, SUB 1262

In the Matter of:	)	
	)	**REBUTTAL TESTIMONY OF**
Petition of Duke Energy Carolinas, LLC	)	**THOMAS J. HEATH, JR.**
And Duke Energy Progress, LLC for	)	**FOR DUKE ENERGY**
Issuance of Storm Cost Recovery Financing	)	**CAROLINAS, LLC AND DUKE**
Orders	)	**ENERGY PROGRESS, LLC**

I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Thomas J. Heath Jr. My current business address is 550 South Tryon Street, Charlotte, North Carolina 28202.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by Duke Energy Business Services, LLC, a service company affiliate of Duke Energy Carolinas, LLC ("DEC") and Duke Energy Progress, LLC ("DEP") (collectively, the "Companies") and a subsidiary of Duke Energy Corporation ("Duke Energy"), as Structured Finance Director.

Q. DID YOU PREVIOUSLY FILE TESTIMONY IN THIS PROCEEDING?

A. Yes. I filed direct testimony and exhibits on October 26, 2020.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. The purpose of my rebuttal testimony is to: (1) respond to Saber Partners, LLC's ("Public Staff Consultants" or "Consultants") concept of "best practices" as they relate to the securitization proposals in these dockets; (2) explain the Statutory Cost Objectives[1] of N.C. Gen. Stat. § 62-172 (the "Securitization Statute") and how DEC and DEP's proposals are consistent with those objectives; (3) explain the Companies' position on post-financing order procedures; (4) respond to the Public Staff's proposals related to return on invested capital and on-going financing expenses; and (5) respond to certain

[1] *See* Duke Energy Carolinas, LLC and Duke Energy Progress, LLC's Joint Petition for Financing Orders, at 2, Docket Nos. E-7, Sub 1243 and E-2, Sub 1262 (Oct. 26, 2020).

mischaracterizations of the Companies' proposals reflected in the testimony of several Public Staff Consultants' testimony.

Q. ARE YOU SPONSORING ANY EXHIBITS WITH YOUR REBUTTAL TESTIMONY?

A. Yes. The following exhibits are presented in conjunction with my rebuttal testimony for both DEC and DEP:

- Heath Rebuttal Exhibit 1 – All discovery produced by the Companies to the Public Staff
- Heath Rebuttal Exhibit 2 – All discovery produced by the Public Staff to the Companies[2]

As this is the first storm securitization transaction proposed by the Companies before the North Carolina Utilities Commission ("Commission"), the Companies believe that the record in these cases may benefit from the additional information conveyed in responses to data requests. Each of these exhibits were prepared under my direction and control, and to the best of my knowledge all factual matters contained therein are true and accurate.

[2] Note these discovery responses reference attachments provided by the Companies and Public Staff in response to the other parties' discovery requests, but do not contain those actual attachments. The Companies will make these attachments available to the Commission upon request.

II. GENERAL OBSERVATIONS REGARDING THE PUBLIC STAFF CONSULTANTS' TESTIMONY

Q. DO YOU HAVE ANY GENERAL OBSERVATIONS ABOUT THE SCOPE AND SCALE OF THE PUBLIC STAFF CONSULTANTS' TESTIMONY IN THESE DOCKETS YOU WOULD LIKE TO DISCUSS?

A. Yes. I want to comment on two aspects of the Public Staff Consultants' testimony that I think unduly impacts their recommendations and may be based upon unfounded concerns about the Companies' incentives and behavior.

Q. WHAT ARE THESE ASPECTS?

A. The first is how little of the Public Staff Consultants' testimony actually addresses issues germane to the Companies' Joint Petition, the content of the proposed Financing Orders, or the numerous exhibits and attachments to them. Instead, the majority of the Public Staff Consultants' testimony is focused on the purported need for post-financing order involvement by the Public Staff and its outside Consultants in the actual bond issuance process. The second is a disagreement with the asserted justifications for such post-financing order participation.

Q. PLEASE EXPLAIN YOUR FIRST GENERAL COMMENT.

A. It is simply the observation that much of the testimony filed by the Public Staff Consultants is focused on ensuring an active and co-equal role for Public Staff and its Consultants in the actual structuring, marketing, and pricing process for

storm recovery bonds.[3] Candidly, the Companies were expecting testimony that was more focused on recommended changes to the detailed Financing Order provisions, but the testimony we received contained very little of that sort of content and instead focused almost exclusively on ensuring a continuing and, by historic standards unusual, active role for both the Public Staff and its Consultants. Therefore, the Companies have inferred that with the exception of the approximately six main recommendations proposed by the Public Staff and its Consultants, all of which will be addressed by me below and/or in the rebuttal testimony of Companies witnesses Charles N. Atkins II and Melissa Abernathy, the Public Staff propose relatively few modifications to the Companies' proposed Financing Order provisions. Notwithstanding, while we think there may be a role for the Public Staff in post-financing order activities, if the Commission deems such role necessary or helpful, we have serious issues with the unprecedented nature of the recommendations proposed by the Public Staff and its Consultants on this issue in this proceeding.

Q. WHAT IS YOUR SECOND GENERAL OBSERVATION ABOUT THE PUBLIC STAFF CONSULTANTS' TESTIMONY?

A. While the Public Staff did not propose significant modification to the Companies' financing proposal, we believe there is a significant conceptual disconnect between the larger context of the Companies' requests in these

[3] While the Companies do not object to a continuing role of the Commission actively participating in the structuring, marketing, and pricing of bonds in this instance or to an advisory role for the Public Staff, as is explained in more detail later in my testimony, we believe that a continuing and co-equal role for an intervenor such as the Public Staff is problematic and unprecedented in the circumstances, in addition to raising issues around the scope of the Public Staff's statutory authority.

dockets and what the Public Staff proposes regarding the execution of the transaction.

Q. PLEASE EXPLAIN.

A. Duke Energy, including DEC and DEP and its other utility operating companies, has many years of experience in issuing long-term debt to both public and private investors, and I believe it has been successful in doing so. Duke Energy currently has more than $50 billion in outstanding long-term bonds in the public debt markets, an amount equivalent to the cumulative amount of utility securitization bonds issued since their inception in the mid-1990s, and has issued an average of approximately $6 billion annually in the public debt markets each year since 2016. All of these bonds have been authorized, marketed, and issued by Duke Energy with the assistance of their advisors and underwriters utilizing practices that are standard for the issuance of such instruments in recognized markets for long-term debt. None of these issuances have been subject to the direct and active supervision of a commission, except for the 2016 securitization transaction by Duke Energy Florida ("DEF"), and all transactions related to DEC and DEP in particular have been preliminarily approved by this Commission prior to issuance pursuant to the requirements of N.C. Gen. Stat. 62-160 *et seq*. Also, none of the issuances have been subject to the direct and active supervision of intervenors. Further, in every case, the interest and fees associated with these long-term debt issuances have been flowed through to Duke Energy's customers as part of the ratemaking process. To the best of my knowledge, no

state utility commission has ever denied recovery of carrying costs and charges associated with Duke Energy's long-term debt nor has any party ever even suggested to a state utility commission that Duke Energy's costs were imprudent or not otherwise eligible for recovery from customers. In every case, the fundamental terms applicable to these borrowings were established at the time of issuance of the securities and, in every case, Duke Energy utilized their best efforts to minimize the costs inherent in these borrowings, which are ultimately paid for by its utility customers.

Q. ARE THE STORM RECOVERY BONDS PROPOSED FOR ISSUANCE IN THE PENDING DOCKETS MATERIALLY DIFFERENT FROM OTHER LONG-TERM DEBT ISSUANCES BY THE COMPANIES?

A. In my opinion, they are not. While I acknowledge that the structures used and the flow of cash are different than a more customary long-term bond issuance, I do not believe those differences necessitate an entirely different process for approval and issuance of those bonds. I particularly reject the notion, which is repeated often in the Public Staff Consultant's testimony, that DEC and DEP would have anything other than their customers' best interests at heart and in mind when structuring, marketing, and pricing these bonds or are presumptively unsuited to manage the bond structuring, marketing, and pricing process in these circumstances because of alleged conflicts of interest. The fundamental purpose of securitization is to lower customer costs. The Companies are quite capable of managing the issuance of storm recovery bonds in this instance competently and fairly and are ready and willing to certify that such bonds will

be issued in a manner consistent with the lowest cost objectives contained in the Securitization Statute as part of that process.

Q. ARE YOU REJECTING THE CONCEPT OF CONTINUING COMMISSION OR PUBLIC STAFF INVOLVEMENT IN THE ISSUANCE OF STORM RECOVERY BONDS AFTER THE ISSUANCE OF A FINANCING ORDER?

A. Not at all. What I am doing is rejecting the fabricated concerns over potential utility carelessness and lack of customer interest expressed in the recommendations of the Public Staff Consultants and noting the fact that the Companies have a long history of accessing debt markets efficiently, at favorable rates, and of recovering the costs of such transactions from our customers with Commission approval. The notion that the Companies would suddenly alter its very well-established business practices and somehow begin applying a less stringent standard while structuring, marketing, and pricing these bonds simply because of the change in cash flows involved in issuing storm recovery bonds is completely unsupported by any evidence.

Q. WHAT ARE YOU ASKING THE COMMISSION TO DO IN THIS INSTANCE?

A. I am asking the Commission to determine whether and to what extent the specific nature of storm recovery bonds requires a completely different process for structuring, marketing, and pricing as proposed by the Public Staff Consultants in this instance, in light of the history and experience of the Companies and the Commission regarding the issuance of other long-term debt

securities for which customers are ultimately liable, and to implement requirements consistent with their conclusions on this subject. In doing so, I ask that the Commission consider the long, collective histories of DEC and DEP in successfully issuing long-term debt and reject the notion that the Companies will not act in the best interest of their customers if not directly supervised by the Public Staff Consultants with respect to the issuance of storm recovery bonds.

I expect the Commission to determine the nature and extent of supervisory authority it feels is necessary and appropriate in these circumstances but do not want that decision to be made on the basis of alleged risks and assumed inappropriate behavior that is completely unsupported by our experience in engaging in similar transactions over a long period of time.

Q. DO YOU BELIEVE THE COMPANIES' JOINT PETITION AND PROPOSED FINANCING ORDERS MEET THE STATUTORY OBJECTIVES OF THE STORM SECURITIZATION STATUTE?

A. Yes I do. The statute defines two objectives, which the Companies refer to as the "Statutory Cost Objectives": 1) the proposed issuance of storm recovery bonds and imposition and collection of storm recovery charges are expected to provide quantifiable benefits to customers as compared to the costs that would have been incurred [and passed through to customers] absent the issuance of storm recovery bonds and 2) the structuring and pricing of the storm recovery bonds are reasonably expected to result in the lowest storm recovery charge consistent with market conditions at the time the storm recovery bonds are

priced and the terms of the financing ordering. As demonstrated in Abernathy DEC Exhibit 5 and DEP Exhibit 5 in the Joint Petition and updated in Abernathy Rebuttal Exhibits 1 – 3, the Companies have structured a financing that is expected to provide net present value savings of approximately $57.5 million for DEC customers over the life of the storm recovery bonds and approximately $216.2 million for DEP customers over the life of the storm recovery bonds. Furthermore, as described in the direct and rebuttal testimony of Companies witness Atkins, the Companies are proposing a structuring and marketing process that is designed to achieve the lowest storm recovery costs consistent with market conditions at the time the storm recovery bonds are priced and the terms of the financing ordering. Finally, to assist the Commission in evaluating the final terms of the transaction and whether or not the Statutory Cost Objectives were in fact met, the Companies propose an issuance advice letter ("IAL") process which would include certifications from each Company as to the satisfaction of the Statutory Cost Objectives and which would give the Commission final authority over the issuance of the bonds.

Q. YOU PREVIOUSLY MENTIONED THAT THE PUBLIC STAFF AND ITS CONSULTANTS' TESTIMONY CONTAINED LIMITED RECOMMENDED CHANGES TO THE COMPANIES' FINANCING ORDERS. PLEASE LIST THEM.

A. The Public Staff and their Consultants recommend that the Commission:

(1) incorporate into its financing order the alleged "best practices" outlined by the Public Staff Consultants, including (a) creation of a post-financing order

and pre-bond issuance review process, (b) provisions in a financing order that are designed to achieve a lowest cost objective, (c) retention of an independent financial advisor and/or counsel to take part actively in all aspects of the structuring, marketing, and pricing of the bonds;

(2) require certifications from the Companies, the bookrunning underwriters, and the Public Staff Consultants that the structuring, marketing, and pricing of storm recovery bonds in fact achieved the lowest storm recovery charges consistent with market conditions at the time of pricing and the terms of the financing order;

(3) approve oversight by the Commission, the Public Staff and its Consultant through their participation on a bond team, that has joint decision-making authority with the Companies, on all matters related to the structuring, marketing, and pricing of the storm-recovery bonds;

(4) limit the Companies' return on their capital contributions to their respective Special Purpose Entities ("SPEs") to each SPE's actual investment return;

(5) make adjustments to the treatment of up-front financing costs, on-going financing costs, servicing and administration fees and tail-end collections, and allow a second "bite at the apple" on auditing certain of the Companies' underlying storm costs; and

(6) lengthen the proposed amortization period from a 15 to 20-year period.

I will be primarily addressing Public Staff and its Consultants' recommendations (1) through (4) and the adjustments to up-front and on-going financing costs contained in recommendation (5), while Companies witness

Abernathy will be primarily addressing the remaining recommendations in (5) and (6). Public Staff Consultants also question certain aspects of the Companies' proposed structure of the transaction and critique some of the Companies' models and calculations used in support of its Joint Petition. While the Public Staff Consultants do not ultimately recommend changes to the Companies' proposed structure at this time, Companies witnesses Atkins, Abernathy, and I address some of their questions and critiques in our respective rebuttal testimony.

III. SABER PARTNERS CONCEPT OF "BEST PRACTICES"

Q. PLEASE SUMMARIZE THE STEPS THE PUBLIC STAFF CONSULTANTS RECOMMENDED AS "BEST PRACTICES" FOR DEC AND DEP'S SECURITIZATION.

A. As stated in Public Staff Consultants witness Hyman Schoenblum's testimony, the alleged "best practices" include:

(1) Commission participation in the selection of underwriters, legal counsel and other transaction participants and in defining the responsibilities of each party. The Commission acting for itself or through a designee, the Public Staff and their Consultants serving as joint decision-makers with the Companies in all matters relating to the structuring, marketing and pricing of the storm recovery bonds. The Commission should rely on experts who have a duty solely to protect customers;

(2) Commission review and negotiation of all transaction documents and contracts that "could affect future ratepayer costs";

(3) Commission should ensure that all statutory limits which benefit customers are strictly enforced;

(4) Commission should establish procedures to ensure all savings are transferred to customers;

(5) Commission should require that storm recovery bonds are offered to the broadest market possible;

(6) Commission should require transparency in the distribution, in the initial pricing and in the secondary market for the storm recovery bonds;

(7) Commission should direct the Commission's staff and the Public Staff and its Consultants to take part fully and in advance in all aspects of structuring, marketing and pricing the storm recovery bonds and direct the financial advisor to disapprove any decision that would not result in the lowest all-in cost of fund and the lowest storm recovery charges;

(8) Commission should require certifications from the underwriters, the Companies and the Public Staff's Consultants as to actions taken to achieve the lowest costs of funds and the lowest storm recovery charges under market conditions at the time of pricing; and

(9) Commission should have authority to enforce the provisions of the financing order and the transaction documents for the benefits of customers.[4]

[4] Direct Testimony of Hyman Schoenblum Senior Advisor – Saber Partners, LLC, at 51-56, Docket Nos. E-2, Sub 1262 and E-7, Sub 1243 (Dec. 21, 2020).

Q. DO YOU AGREE WITH THE CONSULTANTS' RECOMMENDED PRACTICES?

A. Many of them. In fact, contrary to statements made by Public Staff Consultants' witnesses[5], many of these recommended "best practices" have already been incorporated into the Companies' proposed Financing Orders as they were practices utilized in the DEF transaction. I go through them below. However, some additional "best practices" recommended by witness Schoenblum were not present in the DEF transaction and we believe are not appropriate for the Companies' transactions in these dockets, which I will address in more detail below.

Further, some of these "best practices" do not adhere to the statutory framework of the Securitization Statute and deviate from standard North Carolina regulatory practices. Additionally, the Companies do not agree with the Public Staff Consultants that these are standard "best practices" generally agreed upon by the utility industry or the debt capital markets more broadly, but rather are the Public Staff Consultants' "best practices" based upon their evolving personal preferences for these type of transactions. For these reasons, I will refer to them as the Public Staff Consultants' practice recommendations moving forward. Regardless, as I describe further below, the Companies have

[5] *Id.*; Direct Testimony of Joseph S. Fichera, Chief Executive Officer of Saber Partners, LLC, at 37-38, Docket Nos. E-2, Sub 1262 and E-7, Sub 1243 (Dec. 21, 2020); Direct Testimony of Rebecca Klein, Principal of Klein Energy LLC, at 14, Docket Nos. E-2, Sub 1262 and E-7, Sub 1243 (Dec. 21, 2020); Direct Testimony of William B. Moore, Consultant at Saber Partners, LLC, at 14-15, Docket Nos. E-2, Sub 1262 and E-7, Sub 1243 (Dec. 21, 2020); Direct Testimony of Paul Sutherland, Senior Advisor at Saber Partners, LLC, at 42, Docket Nos. E-2, Sub 1262 and E-7, Sub 1243 (Dec. 21, 2020).

already adopted several of them and are not opposed to others that are not inconsistent with the Securitization Statute or commonly used in transactions of this nature. Specifically:

(1) Consultants' Practice Recommendation #1: As discussed later in my rebuttal, the Companies do not object to the formation of a bond team that, *consistent with the DEF transactions referenced by the Public Staff Consultants*[6], includes the Companies, their advisors and counsel, the Commission and its independent outside consultants and/or counsel ("Bond Team"). However, the Companies do object to Public Staff Consultants' repeated plea that it too be given a formal position on such a Bond Team and for the Bond Team to have joint decision-making responsibility. The Companies have grave concerns with an arrangement that allows an intervening party to have a formal role in a financial transaction that, by statute, is required to be performed by the Companies, decided by the Companies, and executed by the Companies. In the DEF transaction, which the Public Staff Consultants repeatedly reference[7] as the model for these transactions, no intervening party was a member of the bond team, and witness Paul Sutherland's testimony concerning "best practices" in that transaction did not recommend any intervenors or their advisors be invited to join the Bond Team as members.[8] Furthermore, I am not aware, and from reviewing the responses to DEC and DEP's discovery requests, it does not

[6] Fichera, at 28.
[7] *Supra,* at note 5.
[8] The Public Staff Consultants were the Florida Public Service Commission's advisors in that transaction.

appear that Public Staff Consultants' witnesses are aware, of *any* example where an intervenor was a member of a similarly constructed bond team.

In addition to the creation of the Bond Team, should the Commission desire, the Companies are not opposed, consistent with the DEF transaction, to a member of the Commission staff (or a Commissioner) being a designated joint decision-maker in matters along with a designated representative of the Companies concerning the structuring, marketing, and pricing of the bonds.[9] The Companies have less concerns with this approach given the Commission's role in regulating the Companies, the Commission's responsibilities under the Securitization Statute, and the use of this framework in the DEF transaction and other utility securitizations across the country. Again, however, the Companies are strongly opposed to the recommendation that an intervening party, even the Public Staff or its Consultant be given a joint decision-making role in the transaction.

(2) Consultants' Practice Recommendation #2: The Companies already included forms of the proposed transaction documents as exhibits to their Joint Petition for review by the Commission.

(3) Consultants' Practice Recommendation #3: The Companies agree that the Commission should adhere to and enforce the Securitization Statute.

[9] Except those recommendations that in the sole view of the Companies would expose the Companies or the SPEs to securities law and other potential liability (i.e., such as, but not limited to, the making of any untrue statement of a material fact or omission to state a material fact required to be stated therein or necessary in order to make the statements made not misleading) or contractual law liability (e.g., including but not limited to terms and conditions of the underwriter agreement(s)).

(4) Consultants' Practice Recommendation #4: The Companies proposed a transaction that will provide significant quantifiable benefits to customers in connection with the Companies' recovery of prudently incurred storm recovery costs, and the true-up mechanism is designed to ensure that storm recovery charges are only collected in amounts necessary to pay principal, interest and financing costs. There cannot and will not be an "economic windfall" to the Companies as a result of the proposed transaction.

(5) Consultants' Practice Recommendation #5: As further described in witness Atkins's testimony, the Companies are structuring the transaction to appeal to a wide array of investors and will broadly market the securities. The Companies have requested flexibility from the Commission to have the ability to structure the transaction to achieve the Statutory Cost Objectives.

(6) Consultants' Practice Recommendation #6: The Companies invite the Commission and/or its outside consultant and counsel to fully participate in the pricing process, including participation on any pricing calls so there is full transparency.

(7) Consultants' Practice Recommendation #7: As previously noted in response to the first recommendation, the Companies support the establishment of a Bond Team to participate in the structuring, marketing and pricing of the storm recovery bonds. Furthermore, a member of the Commission staff (or a Commissioner) along with a designated representative of the Companies, will be joint decision-makers. The Companies recommend, in accordance with Consultants' Practice Recommendation #3 above, that the Commission

adhere to the statutory standard with respect to obtaining the lowest storm recovery charges consistent with market conditions at the time of pricing and terms of the applicable Financing Order as opposed to adopting a different "lowest all-in cost of funds" standard as suggested by witness Schoenblum[10], or an "unqualified lowest storm recovery charge standard" as suggested by witness Rebecca Klein[11]. As mentioned above, the Companies also object to the Public Staff Consultants' request to expand upon the "best practices" and processes used in Florida to create a space for the Public Staff and its Consultants on the Bond Team or for the Public Staff or its Consultants to be a joint decision-maker.

(8) Consultants' Practice Recommendation #8: The Companies have proposed to deliver certifications as described by witness Schoenblum. To the extent other parties offer certifications to the Commission, the Companies do not suggest the Commission ignore them, but these other intervenor certifications should not be conditions to approving the IAL.

(9) Consultants' Practice Recommendation #9: The proposed transaction documents filed with the Commission are modeled off the DEF transaction documents, which have the enforcement provisions suggested by witness Schoenblum.

[10] Schoenblum, at 53.
[11] Klein, at 14.

IV. NORTH CAROLINA STATUTORY COST OBJECTIVES

Q. DOES THE SECURITIZATION STATUTE OUTLINE A LOWEST COST OBJECTIVE FOR THE BOND ISSUANCE?

A. Yes. N.C. Gen. Stat. § 62-172 requires (1) that the issuance of the storm recovery bonds and the imposition and collection of a storm recovery charge are expected to provide quantifiable benefits to customers as compared to the costs that would have been incurred absent the issuance of the storm recovery bonds and (2) that the structuring and pricing of the storm recovery bonds are reasonably expected to result in the lowest storm recovery charges consistent with market conditions at the time the storm recovery bonds are priced and the terms set forth in such financing order.

Q. HOW DO THE COMPANIES RECOMMEND ADHERING TO THESE STATUTORY OBJECTIVES?

A. As proposed in their Joint Petition, the Companies have outlined several steps they will undertake in connection with the structuring, marketing and pricing of the storm recovery bonds. This includes hiring a diverse group of underwriters, conducting broad marketing to attract a wide array of both corporate and more traditional asset backed investors, and crafting disclosure to convey the superior credit quality of the storm recovery bonds. After pricing, each Company intends to provide a certification that the offering of storm recovery bonds provide quantifiable benefits to customers of each Company as compared to the costs that would have been incurred absent the issuance of storm recovery

bonds and that the structuring[12] and pricing of the storm recovery bonds result in the lowest storm recovery charges payable by the customers of such Company consistent with market conditions at the time such storm recovery bonds are priced and the terms set forth in the applicable Financing Order. The Companies will not price the storm recovery bonds unless they are comfortable that they can deliver the proposed certifications.

Q. PUBLIC STAFF CONSULTANTS SEEM TO RECOMMEND ESTABLISHING MORE STRINGENT LOWEST COST STANDARDS THAN THE SECURITIZATION STATUTE PROVIDES FOR, IS THIS CONSISTENT WITH YOUR UNDERSTANDING OF THE INTENT OF THE SECURITIZATION STATUTE?

A. No. Public Staff Consultant Fichera suggests that the Commission create a new standard of the "lowest possible storm-recovery charges and the greatest possible ratepayer protections," while witness Schoenblum suggests, "lowest all-in cost of funds and the lowest storm recovery charges to ratepayers," and witness Klein suggests an "unqualified lowest storm recovery charge standard."[13] However, the Statutory Cost Objectives in the Securitization Statute are clear. Therefore, to the extent that the Public Staff Consultants'

[12] The Public Staff Consultants argue that the Companies did not include in its proposed process the ability for Commission involvement in the marketing of the bonds. As I generally mentioned earlier, the Companies' proposal was designed to be consistent with the plain language of the Securitization Statute, and Section (b)(3)b.3 excludes, from the Commission's requirement to make findings about whether the Statutory Cost Objectives have been met, the marketing phase of the bonds. While the Companies' lawyers have advised me that, in North Carolina, legislative intent is derived from the plain language of the statute, the Companies take no issue with and waive any objection to the Commission's active involvement in the marketing of the bonds if that is what the Commission desires.

[13] Fichera, at 24; Schoenblum, at 53; Klein, at 14.

testimony recommends that the Commission establish a standard more stringent than the one established by the statute, the Commission should not agree to establish one. As Public Staff witness Klein acknowledges in her testimony, "there are no absolutes in this world."[14]

Further, the Public Staff Consultants seem to suggest that a more stringent lowest cost standard can be applied using the "catch-all provision" provided in N.C. Gen. Stat. § 62-172(b)(3)b.12., which states that the Commission may include in its financing order "[a]ny other conditions *not otherwise inconsistent with this section* that the Commission determines are appropriate." Accordingly, the Companies' lawyers have advised me that this provision cannot be used as a "catch all" to expand the scope of the Securitization Statute or create conditions in a financing order that do not adhere to the plain terms and requirements of the Securitization Statute. Based on this guidance and my own review of the Securitization Statute, it is my opinion that the Securitization Statute very clearly establishes the precise cost standard that should be applied, and applying a more stringent standard would be inconsistent with the plain language of the Securitization Statute.

Regardless, the Companies have already proposed to certify to a lowest cost standard after the pricing when the actual terms of the transaction are known to demonstrate the Companies' commitment to get as close as it

[14] Klein, at 17.

reasonably can to such a standard. This is evident on Attachment 8 to Appendix C of the Companies' proposed Financing Orders, which states the following:

> Based on the statutory criteria and procedures, the record in this proceeding, and other provisions of this Financing Order, [DEC/DEP] certifies the statutory requirements for issuance of a financing order and Storm Recovery Bonds have been met, specifically that the issuance of the SRB Notes and underlying Storm Recovery Bonds on behalf of [DEC/DEP] and the imposition and collecting of storm recovery charges authorized by this Financing Order provide quantifiable benefits to customers of [DEC/DEP] as compared to the costs that would have been incurred absent the issuance of Storm Recovery Bonds and that the structuring[15] and pricing of the SRB Notes and underlying Storm Recovery Bonds issued on behalf of [DEC/DEP] *result in the lowest storm recovery charges payable by the customers of [DEC/DEP] consistent with market conditions at the time such SRB Notes and underlying Storm Recovery Bonds are priced and the terms set forth in the Financing Order*. (p. 3)

Q. DO THE COMPANIES HAVE A LEGAL OBLIGATION TO ADHERE TO THE STATUTORY COST OBJECTIVES?

A. Of course we do and, again, on top of that we will certify that they are achieved in the issuance of the bonds.

Q. AS A DUKE ENERGY EMPLOYEE AND PARTICIPANT IN THE BOND ISSUANCES, CAN YOU CERTIFY THAT THE COMPANIES WILL ACHIEVE THE STATUTORY COST OBJECTIVES AND ADHERE TO THE FINANCING ORDERS ONCE ISSUED?

A. Yes. I can certify to that in principle. However, I will have that knowledge and ability at the end of the bond issuance process utilizing the practices and

[15] *See supra,* at note 12.

procedures we customarily use, which are standard in the utility industry and the broader public debt markets.

V. POST-FINANCING ORDER COMMISSION INVOLVEMENT

A. Statutory Background and North Carolina Regulatory Practice

Q. DOES THE STORM SECURITIZATION STATUTE CONTEMPLATE COMMISSION OR INTERVENOR INVOLVEMENT POST-ISSUANCE OF A FINANCING ORDER?

A. No. I am not a lawyer, but I have read the Securitization Statute and I do not see anything appearing to require that securitization be handled in this totally unique way. To me, under the plain language of the Securitization Statute, the financing order is the primary vehicle through which the Commission is anticipated to supervise the issuance of storm recovery bonds. This approach is also completely consistent with the manner in which the Commission handles other topics of significance to utility customers in North Carolina. And while the Companies acknowledge that the Commission has substantial discretion with regard to how it implements the Securitization Statute in this case, it is my opinion that the process suggested by the Public Staff Consultants is not anticipated by the underlying statutory provisions.

Q. BEYOND THE SECURITIZATION STATUTE, ARE YOU AWARE OF ANY NORTH CAROLINA LAW OR RULE THAT ALLOWS THE PUBLIC STAFF AND OTHER INTERVENORS TO DIRECTLY PARTICIPATE IN A PUBLIC UTILITY'S DAY TO DAY ACTIVITIES, SUCH AS BOND ISSUANCES?

A. No. It is my understanding that the historic relationship between regulated public utilities in North Carolina is that a publicly held utility is allowed to operate as a normal corporation except with regard to where its activities touch upon the public interest inherent in the provision of monopoly utility service to the public. Historically, it is my understanding and experience that this framework has involved preliminary approval, and supervision of, the recovery of long-term debt costs, but has not involved direct transactional supervision of discrete aspects of a particular debt offering, which are aspects generally left to the corporations to manage.

Q. IS IT COMMON NORTH CAROLINA REGULATORY PRACTICE FOR THE COMMISSION TO BE INVOLVED IN THE DAY TO DAY ACTIVITIES OF A PUBLIC UTILITY POST-ISSUANCE OF A FINAL ORDER?

A. No. In my opinion, the normal paradigm involved in the Commission's regulation of utilities in North Carolina is to address individual matters subject to the Commission's jurisdiction through administrative hearing procedures. These typically involve filings by the utilities that initiate a proceeding followed by a pre-filed testimony and evidentiary hearing process that results in a final

Commission order. Upon issuance of the final order in such proceedings, the options available to the parties are to comply with the order, to ask for reconsideration of the order, or to appeal the order to the North Carolina Appellate Courts. I am not familiar with any prior proceeding where this Commission has exercised active and ongoing implementation supervision of corporate transactional activities after the issuance of a final order.

Q. IS IT COMMON NORTH CAROLINA REGULATORY PRACTICE FOR INTERVENORS TO BE INVOLVED IN THE DAY TO DAY ACTIVITIES OF A PUBLIC UTILITY POST-ISSUANCE OF A FINAL ORDER?

A. No. In this regard, what has been proposed by the Public Staff Consultants in this proceeding is extraordinary.

Q. WHAT SECURITIES LAW LIABILITY CONCERNS DO YOU HAVE WITH THE PROPOSAL THAT THE PUBLIC STAFF AND ITS CONSULTANTS, OR ANY OTHER INTERVENOR NOW OR IN THE FUTURE FOR THAT MATTER, REMAIN AN ACTIVE PART OF THE BOND ISSUANCE PROCESS AFTER THE FINANCING ORDER IS ISSUED IN THIS CASE?

A. Under federal securities law, DEC and DEP will be the issuers of the underlying bonds in this instance and as such will have all the obligations under the federal securities laws with regard to such issuances. To the extent that the Public Staff and its Consultants and/or other intervenors, now or in the future, remain actively involved in the structuring, marketing, and pricing of bonds, the

Companies have concerns about how that impacts their potential liabilities under the securities laws and to what extent such activities could expose the Public Staff and other intervenors, now or in the future, to potential liability.

B. The Companies' Initial Proposal

Q. EVEN THOUGH THE SECURITIZATION STATUTE DOES NOT CONTEMPLATE COMMISSION OR INTERVENOR INVOLVEMENT POST-ISSUANCE OF A FINANCING ORDER, AND DESPITE THE CONCERNS IDENTIFIED ABOVE, DID THE COMPANIES CONSIDER THE COMMISSION BEING INVOLVED POST-ISSUANCE OF THE FINANCING ORDERS?

A. Yes.

Q. WHY DID THE COMPANIES PROPOSE THE OPTION TO THE COMMISSION TO BE INVOLVED POST-ISSUANCE OF THE FINANCING ORDERS?

A. Because the actual structure and pricing of the bonds will not be known upon the issuance of the Financing Orders, DEC and DEP believed it was not unreasonable to offer the option of Commission involvement post-issuance of the Financing Orders, if the Commission chose, so that it can be comfortable the transaction satisfies the requirements of the Securitization Statute. The Companies did not want to presume in their Joint Petition what level of post-financing order involvement the Commission might ultimately wish to undertake. Therefore, the Companies' proposal for the IAL process was designed to allow the Commission to determine whether and to what extent it

wanted to be involved once the Financing Orders are issued. DEC and DEP's proposal in no way seeks to limit the role of the Commission to oversee the proposed transaction.

Q. PLEASE DETAIL THE COMPANIES' INITIAL PROPOSAL WITH RESPECT TO A DESIGNATED COMMISSIONER OR MEMBER OF COMMISSION STAFF.

A. The Companies proposed an IAL process that provided for a designated Commissioner or member of Commission staff to be involved post-issuance of the Financing Orders. The proposed IAL process additionally included objectively measurable criteria by which the Commission can assess whether the Statutory Cost Objectives of the proposed transactions were achieved. These criteria include whether:

1) the issuance of the storm recovery bonds and imposition and collection of storm recovery charges as authorized in the Financing Orders provide quantifiable benefits to customers as compared to the costs that would have been incurred absent the issuance of storm recovery bonds; and
2) the structuring and pricing of the storm recovery bonds, including the issuance of SRB Securities, resulted in the lowest storm recovery charges consistent with market conditions at the time the storm recovery bonds are priced and the terms set forth in the Financing Orders.

The IAL process proposed by the Companies is similar to the IAL process used in the DEF transaction.

C. The Public Staff's Proposed Bond Team

Q. PLEASE DETAIL THE PUBLIC STAFF'S BOND TEAM PROPOSAL.

A. The Public Staff's bond team proposal calls for the Public Staff and its Consultants to be joint decision-makers with the Companies and the Commission in all aspects of the proposed transaction.

Q. WHAT ARGUMENTS DOES THE PUBLIC STAFF MAKE IN SUPPORT OF ITS PROPOSED BOND TEAM?

A. The Public Staff and its Consultants claim that they, and only themselves, are working for the interest of customers with respect to the proposed transaction and therefore they must be a joint decision-maker with respect to the proposed transaction.[16]

Q. DOES THE PUBLIC STAFF OR ITS FINANCIAL ADVISOR HAVE ANY EXPLICIT LEGALLY BINDING FIDUCIARY OBLIGATION TO CUSTOMERS?

A. While the Public Staff's financial advisor claims it has an implicit fiduciary obligation, the fact is that neither the Public Staff nor its financial advisor has any explicit legally binding fiduciary obligation to DEC and DEP's customers. For example, in response to the Companies' Data Request No. 2-33, which asked "Does Saber Partners' contract with the Public Staff expressly create a

[16] Direct Testimony of Brian A. Maher, at 17, Docket Nos. E-2, Sub 1262 and E-7, Sub 1243 (Dec. 21, 2020).

legally binding fiduciary duty to North Carolina customers or anyone else," Public Staff Consultant witness Maher objected to the question, and simply referenced the following question and answer in his testimony:

> **Q. Are you giving an opinion as to whether there is a legal requirement of any party in this transaction to have a fiduciary relationship?**
>
> A. No. I am discussing the important issues related to whether a fiduciary relationship exists and what the Commission should consider in deciding how to evaluate information it receives from different parties to the proposed transaction.

It is unclear to the Companies how the Public Staff's Consultants repeatedly claim a fiduciary duty to North Carolina utility customers with respect to the securitization transaction, but simultaneously fail to testify as a matter of fact that they have an actually established, legally binding fiduciary duty to North Carolina utility customers.

Q. DO YOU BELIEVE THE PUBLIC STAFF HAS THE LEGAL RIGHT TO BE JOINT DECISION-MAKERS IN THE PROPOSED TRANSACTION?

A. No. It would not be appropriate for an intervenor to be a joint decision-maker in any securities offering of a public utility, including this type of securities offering. As noted by Public Staff witness Klein, N.C. Gen. Stat. § 62-15(d) states the Public Staff has a responsibility to "[i]ntervene on behalf of the using and consuming public," but this does not mean it should be making decisions on behalf of a public utility company following finalization and issuance of a Commission order. Such joint decision-making authority is inconsistent with

Public Staff's statutory mission or its traditional role in North Carolina. In addition, the Companies reviewed the record of other utility securitization transactions and could not find any other examples where an intervenor had a comparable joint decision-making role. Notwithstanding the testimony submitted by Public Staff Consultants' witnesses and responses to discovery requests, none of the Public Staff Consultants' witnesses, including witness Klein, can cite an example of an intervenor being a joint decision-maker in a utility securitization bond offering.

The structure that the North Carolina legislature selected in adopting N.C. Gen. Stat. § 62-172 involves the public utility or an assignee of the public utility as the issuer of the storm recovery bonds. As a result, primary securities law liability and contractual liability rests with the public utility and its assignee and not with the State of North Carolina or with any intervenor to the proceeding. Unlike the Companies, the intervenors have no liability and therefore should not be in position of any joint decision-making authority.

Furthermore, while the Commission and the State of North Carolina have ongoing obligations pursuant to the Securitization Statute, including to support the true-up mechanism and to uphold the state pledge, intervenors have no such obligations or authority. Further, by allowing an intervening party – even the Public Staff – to have joint decision-making authority in the transaction, it is unclear to the Companies how the effect of setting that precedent will impact the inclusion or exclusion of other intervening parties who may want to participate in future transactions. A simple example of this

concern is the possibility that in a future securitization the Attorney General – who is also statutorily charged with representing the using and consuming public – may seek participation in decision-making but may have different goals and desires than the Public Staff. The potential for disagreements between the Public Staff and the Attorney General – both of whom represent the same clients – is a well-known phenomenon in regulatory proceedings before the Commission.

Q. DO YOU BELIEVE THE STORM COST SECURITIZATION TRANSACTION IS SIGNIFICANTLY "MORE COMPLEX" THAN OTHER PUBLIC UTILITY TRANSACTIONS UNDERTAKEN BY DEC AND DEP AS THE PUBLIC STAFF CONSULTANTS SUGGEST?

A. No. As I explained earlier, DEC and DEP recognize and respect the unique aspects of utility securitization bonds in general and more specifically the added features of the proposed SRB Securities transaction. However, the Companies do not accept the Public Staff Consultants' assertion that the proposed transaction is significantly "more complex" than other sophisticated debt transactions undertaken by them. While the proposed transaction does involve certain unique aspects and structural considerations, it is still at its most fundamental level the issuance of publicly issued debt to institutional investors. Moreover, the assertion that the transaction is generally "more complex" is subjective and does not in and of itself evidence a need for the Public Staff Consultants, or other intervenors, to be joint decision-makers in the transaction.

Q. PLEASE DETAIL THE COMPANIES' EXPERIENCE AS ISSUERS IN THE PUBLIC DEBT MARKETS.

A. As I briefly referenced earlier, DEC and DEP, their affiliates, and parent company are frequent issuers in the public debt markets. Any implication by the Public Staff Consultants that Duke Energy is not a sophisticated market participant or does not know how to evaluate securities offerings and challenge its underwriting banks is without merit and baseless. Given his 40 years of experience covering the U.S. utilities sector in general and Duke Energy in particular[17], I think Public Staff Consultants witness Barry M. Abramson would agree that Duke Energy's depth of experience with issuing public debt and the related selection of underwriters and other transaction participants has not been questioned in any of its regulated jurisdictions. In addition, through DEC and DEP affiliate DEF's 2016 transaction, Duke Energy's treasury team, which included me, have direct and relevant experience with the issuance of utility securitization bonds. Further, we have already engaged several key participants in DEF's 2016 transaction team, who are participating in DEC and DEP's proposed transaction including Hunton Andrews Kurth LLP as issuer counsel, Guggenheim Securities, LLC as co-advisor (who was recommended by Saber Partners, LLC in the DEF transaction), and Paul, Weiss, Rifkind, Wharton & Garrison LLP as structuring advisor counsel and also eventually underwriter counsel (again by recommendation of Saber Partners, LLC in the DEF

[17] Direct Testimony of Barry M. Abramson, at 3-4, 11, Docket Nos. E-2, Sub 1262 and E-7, Sub 1243 (Dec. 21, 2020).

transaction). Based on these collective factors, DEC and DEP's intention to structure and market their proposed transaction in much the same manner as DEF's 2016 transaction, and the active role permitted to a designated Commissioner or member of Commission staff, if the Commission desires, as outlined in the Joint Petition and further addressed in the remainder of my rebuttal testimony will ensure the proposed transaction meets the Statutory Cost Objectives.

In addition, since the beginning of 2019, DEC and DEP have issued a combined total of $3.6 billion in the public debt market across seven tranches of debt. Every one of these tranches were allocated to an average of over 65 unique investor accounts, with one of the tranches allocated to 105 unique accounts. By comparison, DEC and DEP affiliate DEF's 2016 securitization issuance allocated $1.294 billion across five tranches to 56 unique accounts. It is evident that DEC and DEP have a demonstrated track record of broad investors outreach and marketing and have no incentive or intention to operate outside of our customary business practices.

Q. WHAT HAS BEEN THE COMMISSION'S INVOLVEMENT IN THESE TRANSACTIONS?

A. The Commission, on a preliminary basis, authorized the issuance of the debt and required reporting of the details of the terms of the debt issuances but otherwise played no role in negotiating or issuing the actual instruments.

Q. DID THE COMPANIES CONSIDER CUSTOMERS' INTERESTS DURING THESE TRANSACTIONS?

A. Yes, of course. The Companies are keenly aware that the costs of their debt issuances are subject to ultimate recovery from customers and it is not in the Companies' best interests to do anything that unnecessarily adds to the cumulative costs of electric service that their customers must pay. This is as true of their past issuances as it is of the current pending bond transactions. Further, the Companies strongly reject any assertion from the Public Staff Consultants that DEC or DEP would enter into any transaction without due consideration of the transaction's impact on their customers or without considering their customers' perspectives.

D. <u>Adoption of a Bond Team at Commission Discretion</u>

Q. DID THE PUBLIC STAFF LOOK TO THE DEF 2016 SECURITIZATION PROCEEDING AS PRECEDENT FOR THIS NORTH CAROLINA PROCEEDING AND THEIR BOND TEAM PROPOSAL?

A. Yes. Witness Joseph S Fichera references the DEF transaction extensively[18] and other Public Staff Consultants reference it as well. That being said, Public Staff Consultants do not describe the bond team or joint decision-making authority from Florida accurately. To start with, witness Fichera incorrectly

[18] *See, e.g.,* Fichera, at 28; Abramson, at 11; Klein, at 11, Exhibit 2, Exhibit 4; Maher, at 12-13, Exhibit 1; Schoenblum, at 11, 27-28, 31, Exhibit 1; Sutherland, at 12-13, Exhibit 7; Direct Testimony of Steven Heller, President of Analytical Aid – Saber Partners, LLC, at 11, 14, Docket Nos. E-2, Sub 1262 and E-7, Sub 1243 (Dec. 21, 2020).

states that DEF did not propose bond team in Florida. To clarify the record, DEF's proposed financing order attached to its petition stated, "[the] Commission, as represented by a designated Commissioner, designated Commission Staff, the Commission's financial advisor, and the Commission's outside legal counsel (if any), shall be actively involved in the bond issuance…as part of a Bond Team that also includes DEF, its financial advisor or underwriter(s), and its outside counsel(s), in the structuring, marketing, and pricing of each series of nuclear asset-recovery bonds."[19]

In addition, the bond team did not have joint decision-making authority with DEF. Instead, a designated representative from DEF and a designated representative of the Commission were joint decision-makers. Finally, witness Fichera incorrectly describes the role of the Commission to resolve disputes.[20] Witness Fichera testified that a designated commissioner was selected to resolve bond team disputes, but the process was only limited to resolving disputes among the joint decision-makers, not disputes among the entire bond team.[21]

[19] See Duke Energy Florida, Inc.'s Petition for a Financing Order and Motion to Consolidate, at 28, Docket No. 150171-EI (July 27, 2015).
[20] Fichera, at 31.
[21] *See* Florida Public Service Commission's Financing Order No. PSC-15-0537-FOF-EI, at 58, Ordering ¶ 67, Docket No. 150171-EI (Nov. 19, 2015) ("Florida Financing Order").

Q. TO CLARIFY, IS THE PUBLIC STAFF CONSULTANTS' PROPOSAL FOR A BOND TEAM ACTUALLY INCONSISTENT WITH THE DEF BOND TEAM PROPOSAL IT RELIES UPON AS PRECEDENT FOR ITS PROPOSAL?

A. Yes. The Public Staff Consultants' proposal for a bond team goes beyond the bond team used in the DEF transaction by recommending an intervening party, the Public Staff, be included as a member of the Bond Team and have joint decision-making authority. Membership on the DEF bond team was limited to DEF and its financial advisor and designees of the Florida Public Service Commission, including their financial advisor (i.e., Saber Partners, LLC).[22] Bond team membership was not extended to any intervening party to the financing proceeding. Representatives of the customer advocate (Office of Public Counsel) were invited to and joined certain of the bond team calls as a courtesy, however, they were not part of the bond team and did not have a formal role in the post-financing order stage of the DEF transaction. Other transaction participants (legal counsel, underwriters, etc.) were also invited to participate in the bond team calls but none of these parties were members of the bond team. Furthermore, as noted above, there was no joint decision-making authority among all of the members of the DEF bond team, it was limited to the designated representative of DEF and designated representative of the Florida Public Service Commission.

[22] Florida Financing Order, at 54, Ordering ¶ 38.

In the Public Staff Consultants' response to the Companies' Data Request No. 2-4, the Consultants seemed to intentionally try to make the DEF bond team broader than it actually was by stating "[i]n the 2016 nuclear asset-recovery bond transaction for DEF, however, Florida PSC's financing order established a [b]ond [t]eam consisting of DEF and its designated advisors, the Florida PSC and its designated advisors, legal counsel, and representatives to oversee and approve post-financing order decisions concerning the structuring, marketing and pricing of those securitized bonds." This is simply incorrect. The DEF financing order actually states "DEF, its structuring advisor, and designated Commission staff and its financial advisor will serve on the Bond Team." Regarding decision-making authority, the DEF financing order states "[o]ne designated representative of DEF and one designated representative of the Commission shall be joint decision makers for all matters concerning the structuring, marketing, and pricing of the bonds except for those recommendations that in the sole view of DEF would expose DEF or the SPE to securities law and other potential liability (i.e., such as, but not limited to, the making of any untrue statement of a material fact or omission to state a material fact required to be stated therein or necessary in order to make the statements made not misleading) or contractual law liability (e.g., including but not limited to terms and conditions of the underwriter agreement(s))."

Q. WHAT IS THE POINT YOU WANT THE COMMISSION TO DERIVE FROM YOUR EXPLANATION OF THE CONSTRUCT OF THE DEF BOND TEAM?

A. In the event the Commission decides to weigh the applicability of the construct of the DEF bond team model to the Companies' proposed transaction in this case, I want to make clear to the Commission that the Public Staff Consultants did not accurately explain the construct of the DEF bond team, which the Public Staff Consultants heavily rely on in their testimony. My explanation further highlights the point I made earlier that the composition of the bond team the Public Staff Consultants are recommending in these cases has not been adopted in any utility securitization anywhere in the country of which I am aware, including in the referenced DEF transaction.

Q. ARE THE COMPANIES WILLING TO ADOPT THE DEF BOND TEAM MODEL?

A. Yes. While the Companies believe this is ultimately a decision for the Commission, the Companies would support a Bond Team comprised of the Companies, their advisor(s) and counsel, and a designated Commissioner or member of Commission staff, including any independent consultants or counsel hired by the Commission to ensure that the structuring, marketing[23], and pricing of the storm recovery bonds will achieve the Statutory Cost Objectives. As I

[23] *See supra,* at note 12.

stated above, this is consistent with the bond team approach used in DEF's transaction.

Q. UNDER THIS MODEL, WHO WOULD HAVE DECISION-MAKING AUTHORITY?

A. Similar to the DEF transaction, a designated representative of the Companies and a member of the Commission or Commission staff, as a designated representative of the Commission, would be joint decision-makers in all aspects of the structuring, marketing, and pricing of the storm recovery bonds except for those recommendations that in the sole view of the Companies would expose either Company or any SPE to liability. Pursuant to federal securities laws, the Companies, in their role as "sponsors" and "depositors", have strict liability for the accuracy of disclosure documents including the prospectus for the storm recovery bonds and any other materials and information delivered to investors. No other parties to the proposed transaction have this liability. Therefore, the Companies must have final say over these items.

Like in Florida, the Companies and a member of the Commission or Commission staff, as a designated representative of the Commission and its outside consultant or counsel, as bond team members, excluding the Companies' structuring advisor, would also have equal rights on the hiring decisions for the underwriters. However, the Companies would like to retain their right to select and engage any counsel for the Companies, the SPEs and the underwriters.

Q. PUBLIC STAFF CONSULTANTS RECOMMEND THE COMMISSION ENGAGE A FINANCIAL ADVISOR; DO YOU AGREE?

A. Ultimately this is a question for the Commission. If the Commission feels that it will be beneficial to engage an outside consultant to assist the Commission in connection with making determinations under the Securitization Statute, there are several firms that have experience advising utility commissions in offerings of utility securitization bonds. The Companies understand, from reviewing prior utility securitization financing orders and transactions, that firms such as Drexel Hamilton, Ducera Partners, Hilltop Securities (formerly First Southwest), Oxford Advisors, and Public Financial Management Company have advised other commissions on current or previous utility securitization transactions. The Companies also believe that larger financial institutions such as, but not limited to, Goldman Sachs, Morgan Stanley, and JP Morgan may have advisory capabilities.

Q. CAN OTHER PARTIES, INCLUDING THE PUBLIC STAFF AND ITS CONSULTANTS, PARTICIPATE IN THE STRUCTURING, MARKETING, AND PRICING OF THE BONDS UNDER THIS MODEL?

A. While they would not be formal members of the Bond Team, the Companies are not opposed to the underwriters or the Public Staff and its Consultants being invited to join all Bond Team meetings. Discussion among the Bond Team, the underwriters and Public Staff will allow for multiple voices and suggestions about the best way to structure, market, and price the storm recovery bonds.

Companies witness Atkins further elaborates on this concept.

E. Certification

Q. PUBLIC STAFF CONSULTANTS ARE PREPARED TO OFFER AN "INDEPENDENT" CERTIFICATION THAT THE TRANSACTION MEETS THE STATUTORY REQUIREMENTS IF THE COMMISSION DESIRES. IS THIS CONSISTENT WITH THE DEF MODEL?

A. No, it is not. Certifications for the DEF transaction were provided by DEF, the Florida Public Service Commission's advisor, and the lead underwriters.

Q. DO YOU BELIEVE ANY CERTIFICATION BY A PARTY OTHER THAN THE COMPANIES IS NECESSARY?

A. No. Unlike the Florida transaction referenced by the Public Staff Consultants witnesses, where DEF was only obligated to certify that "the structuring, pricing and financing costs of the [securitization] bonds and the imposition of the proposed [securitization] charges have a *significant likelihood of resulting in lower overall costs or significantly mitigate rate impacts to customers* as compared with the traditional method of financing and recovering [securitization] costs," the Companies are proposing in connection with the IAL to certify to a higher standard that, based on the actual results after pricing, the structuring and pricing[24] of the SRB Securities and underlying storm recovery bonds issued on behalf of DEC and DEP result in the *lowest storm recovery charges* payable by the customers of DEC and DEP consistent with market

[24] For the reasons explained above, the Companies do not object to certifying that the marketing phase of the bond issuance met the Statutory Cost Objectives as well.

conditions at the time such SRB Securities and underlying storm recovery bonds are priced and the terms set forth in the Financing Orders. As such, it is unclear what value an additional certification could provide that is not already covered by the Companies' proposed certification. To the extent, however, the Commission wishes to obtain a certificate from an independent outside consultant, like the DEF transaction, acceptance of the IAL should not be conditioned on the delivery of certifications from parties other than the Companies.

VI. PUBLIC STAFF ACCOUNTING ADJUSTMENTS

Q. ARE THERE ANY ACCOUNTING RECOMMENDATIONS MADE BY THE PUBLIC STAFF THAT YOU WANT TO ADDRESS?

A. Yes. Public Staff witnesses Michael C. Maness and Michelle M. Boswell jointly propose that the Companies' capital contributions to each respective SPE should be limited to the actual investment return earned by the SPEs on that contribution. Public Staff witnesses Maness and Boswell also recommend that adjustments to on-going financing costs be subject to future prudency reviews by creating a corresponding regulatory liability for the purposes of providing a credit to customers for adjustments the Public Staff deems to be imprudently incurred. I explain why such a proposal is unprecedented, not contemplated by the structure of, and inconsistent with, the Securitization Statute.

Finally, Public Staff witnesses Maness and Boswell propose that over-recoveries of up-front financing costs should be credited back to customers

through use of a deferred regulatory liability and subsequent credit to the Companies' cost of service, in each of the Companies' next general rate cases. Companies witness Abernathy provides a detailed summary of the Public Staff's testimony on this issue, which I will not recite here, and briefly explains why the Public Staff's proposal makes little sense from a ratemaking perspective given the separation between the Companies and each SPE. I further expand on the need for and nature of that separation below.

A. Return on Capital Contribution

Q. DO YOU AGREE WITH PUBLC STAFF WITNESSES MANESS AND BOSWELL THAT THE COMPANIES' RETURN ON ITS CAPITAL CONTRIBUTIONS SHOULD BE LIMITED TO THE ACTUAL RETURN ON FUNDS IN THE COLLECTION ACCOUNTS?

A. No. The Companies are entitled to earn a return on their equity capital contributions to these proposed transactions commensurate with the level of return a regulated utility is otherwise entitled to earn on its equity capital investments. For this reason, the Companies believe that their proposed level of return, equal to the interest rate of the longest maturity bond, is reasonable, justified, and consistent with the recommendation of Saber Partners, LLC in the DEF transaction.

The Companies' cash investment deposited into the capital account is not released to the Companies until after the last payment of the longest tranche of bonds is paid in full, which will be at least 15 years from now and perhaps longer if the Commission decides to extend the maturity of the bond to 20 years

as the Public Staff has proposed. If the Companies were investing this capital in assets that would be added to their respective rate base and amortized over a similar period, it would be entitled to a return at its weighted average cost of capital ("WACC"). However, here, the Companies are actually asking for a level of return that is *less* than its WACC. In fact, the market interest rate on the longest tranche is based upon the weighted average of that tranche, not the market rate for a "bullet" payment that matches the final payment of the longest tranche. As a result, the return proposed to be earned by the Companies is less than a market rate for the date the equity contribution is expected to be returned to the Companies. The plain fact is that the Companies are investing millions of dollars into entities, for the quantifiable benefits for its customers, that will not be returned for potentially two decades. To compensate the Companies for the lost opportunity to invest that capital in assets that would yield a higher return, the Companies are seeking a return that is less than its WACC but higher than what the Public Staff has proposed. Moreover, the Companies are aware that the DEF transaction allowed and utilized the same return proposed by the Companies here. For these reasons, the Companies ask that the Commission allow the Companies to earn its requested return on its capital contributions.

B. <u>On-going Financing Costs</u>

Q. PLEASE REMIND THE COMMISSION WHAT ON-GOING FINANCING COSTS ARE AND HOW THE COMPANIES PROPOSE TO ACCOUNT FOR THEM.

A. As I explain in my direct testimony, there will be on-going expenses that will be incurred by each SPE throughout the life of the storm recovery bonds to support its ongoing operations. These on-going financing costs include servicing fees; administration fees; accounting and auditing fees; regulatory fees; legal fees; rating agency surveillance fees; trustee fees; independent director or manager fees; and other miscellaneous fees associated with the servicing of the storm recovery bonds. Of these on-going financing fees, the largest is the servicing fee, which is approved in the Financing Orders at 0.05% of the initial aggregate principal amount of the storm recovery bonds so long as DEC or DEP, as applicable, or a successor utility is the servicer. Additionally, the administration fee is approved by the Commission in the Financing Orders. The remaining fees are *de minimis* amounts owed to third parties to maintain the structure of the bonds. The SPE's sole source of funds are the storm recovery charges collected from customers. To ensure the amount of storm recovery charges collected for each payment period is sufficient to pay the principal and interest on the storm recovery bonds and the on-going financing costs, they are factored into each true-up adjustment.

Q. PLEASE DESCRIBE THE PUBLIC STAFF'S PROPOSAL REGARDING ON-GOING FINANCING COSTS.

A. In contrast to the Companies' recommendation, the Public Staff recommends that adjustments to on-going financing costs that are paid from the storm recovery charges be matched with an offsetting regulatory asset or liability in the Companies' traditional ratemaking cost of service to create a link to adjust the Companies' cost of service in a future general rate case proceeding upon subsequent audit for prudency review of such adjustments.

Q. SHOULD THE COMMISSION REJECT THE ACCOUNTING TREATMENT FOR ON-GOING FINANCING COSTS PROPOSED BY THE PUBLIC STAFF?

A. Yes. The structure of securitization is simply not designed to work this way and the proposed audit and prudency review is inconsistent with the Securitization Statute. Other than the servicing fee and administration fee payable to DEC or DEP, as applicable, which are approved upfront in the Financing Orders, the remaining costs are third party costs incurred to support the structure. These types of costs are approved in the Financing Orders and IAL, and future adjustments are generally not subject a prudency review over the life of the transaction. The Companies are concerned with the Public Staff's proposed treatment because it is a negative factor in the separateness analysis between the SPE and the Company, which owns the member interest in the SPE. The on-going financing costs are the costs of the SPE, not costs of the applicable utility. Furthermore, witnesses Maness and Boswell improperly

suggest that the Commission should authorize a new audit process that expands both the time and scope of the review permitted by the Securitization Statute. The statute states that any review of an adjustment filing be limited to mathematical and clerical errors and the Commission must inform the Companies of such errors within 30 days of the filing, so their proposal is inconsistent with the plain meaning of the statute.

While the Companies are more than willing to provide the details of on-going financing costs to the Public Staff to be able to check for mathematical or clerical errors in connection with each true-up adjustment, as the statute specifically contemplates, the on-going financing costs should not themselves be subject to the type of prudency review and cost of service impacts contemplated by the Public Staff.

C. Over-Recovery of Up-front Financing Costs

Q. DO YOU AGREE WITH COMPANIES WITNESS ABERNATHY THAT THE PUBLIC STAFF'S PROPOSAL TO ESTABLISH A REGULATORY LIABILITY TO POTENTIALLY ADJUST THE COMPANIES' COST OF SERVICE IN THEIR NEXT GENERAL RATE CASES FOR ANY OVER-RECOVERY OF UP-FRONT FINANCING COSTS DOES NOT MAKE SENSE FROM A REGULATORY PERSPECTIVE?

A. Yes. My discussion above regarding the separateness of the Companies and the SPEs in the context of ongoing financing costs applies here too. If there is an over-collection of up-front financing costs, then it is the SPE – not the

Companies – that will have received an excess of bond proceeds above costs that were actually incurred. As such, it is appropriate for the SPE to lower the storm recovery charge being collected from customers, as a result of the over-collection in connection with the next true-up as the Securitization Statute contemplates.

VII. CONCLUSION

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.