

**STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH**

DOCKET NO. A-41, SUB 22

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

<p>In the Matter of</p> <p>Joint Application of Bald Head)</p> <p>Island Transportation, Inc., Bald)</p> <p>Head Island Limited LLC, and Bald)</p> <p>Head Island Ferry Transportation,)</p> <p>LLC, for Approval of Transfer of)</p> <p>Common Carrier Certificate to Bald)</p> <p>Head Island Ferry Transportation,)</p> <p>LLC, and Permission to Pledge)</p> <p>Assets</p>	<p>PUBLIC STAFF BRIEF</p>
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NOW COMES THE PUBLIC STAFF – North Carolina Utilities Commission (Public Staff), by and through its Executive Director, Christopher J. Ayers, respectfully submits the following:

I. Background

On July 14, 2022, and by amendment on January 24, 2023, Bald Head Island Limited LLC (BHIL), Bald Head Island Transportation, Inc. (BHIT), and Bald Head Island Ferry Transportation, LLC (BHIFT, collectively with BHIL and BHIT, the Applicants), a wholly owned subsidiary of Pelican Legacy Holdings, LLC (Holdings), and to be managed by SharpVue Capital, LLC (SharpVue), filed an Application (as amended, the Application) pursuant to N.C. Gen. Stat. § 62-111 for approval to transfer BHIT's Common Carrier Certificate to BHIFT to operate the passenger ferry transportation services to and from Bald Head Island, the tram

services on the island, and, in addition, the parking, barge, and tug operations (collectively, the Transportation Assets) (the Transfer).¹

As part of their Application, the Applicants have requested Commission permission to pledge assets and borrow or issue debt, pursuant to N.C. Gen. Stat. §§ 62-160 and 62-161, secured by the Transportation Assets as may be necessary to finance the Transfer (the Pledging of Assets, and collectively with the Transfer, the Proposed Transaction).

As set out in a Joint Proposed Order filed today, and the Settlement Agreement and Stipulation (Stipulation) with regulatory conditions (Regulatory Conditions) filed with the Commission on May 10, 2023, the Applicants and Public Staff believe that it is unnecessary to establish the rate base of the regulated parking and barge operations (Parking and Barge Operations) at this time.

Nonetheless, should the Commission decide that it is necessary to establish the rate base of the Parking and Barge Operations, the Public Staff provides this brief to address: 1) the value to be included in rate base for the Parking and Barge Operations, and 2) the appropriateness of allowing Buyers to collect an acquisition adjustment (Acquisition Adjustment)² with respect to the Transportation Assets. The Public Staff recommends that the Commission require the use of net

¹ The parties to the Asset Purchase Agreement are BHIL and BHIT (together, Seller or Sellers) and BHIFT (regulated assets), Pelican Logistics, LLC (non-regulated assets), Pelican Real Property, LLC (real property), and SharpVue (as a signatory) (collectively, Buyer or Buyers). BHIFT, Pelican Logistics, LLC, and Pelican Real Property, LLC, are all wholly owned by Holdings, as is Pelican IP, LLC.

² An Acquisition Adjustment is any amount included in rate base above the net book value established pursuant to N.C. Gen. Stat. § 62-133.

reasonable original cost as the appropriate value to include in rate base for the Parking and Barge Operations and disallow any request for an Acquisition Adjustment. However, the Public Staff also believes that it is highly likely that long-term ground leases for Parking and Barge Operations as contemplated by the Applicants and Public Staff in the Stipulation (Section II Settled Terms, Item C) would serve as a sufficient basis for establishing cost of service rate base. Nonetheless, as noted herein, no such leases have been presented to the Commission, therefore under this scenario, a determination of rate base would be difficult, if not impossible, at this time.

II. Commission's Order in Docket No. A-41, Sub 21

In Docket No. A-41, Sub 21 (Sub 21), the Village of Bald Head Island (Village) filed a Complaint requesting the Commission determine the public utility status of the Parking and Barge Operations. In its December 30, 2022 Order Ruling on Complaint and request for Determination of Public Utility Status (Sub 21 Order), the Commission found that:

. . . [No] party has sought to present evidence on the panoply of matters appropriate for full review or determination in a general rate case. To this end, the Commission agrees with witness Mayfield that this docket is a premature, and improper, forum in which to address such issues.

As a result, and as requested, the Commission treats the Complaint only as a request for a declaration of utility status. The Commission does not treat the Complaint as a request to initiate a rate proceeding and does not require either BHIT or BHIL, separately or jointly, to file a general rate case at this time. *See generally State ex rel. Utils. Comm'n v. Carolinas Comm. for Indus. Power Rates*, 257 N.C. 560, 569-70, 126 S.E.2d 325, 332-33 (1962). Without more

and absent any requested change, the Commission permits the status quo — and the current rates and services of the Parking and Barge Operations — to continue.

Sub 21 Order, 28.

The Commission found that “[t]here is no doubt that these Ferry and Parking Operations not only evolved together but were planned from the outset as necessary components of a single, holistic transportation service as early as 1998” and ultimately concluded that it was in the public interest to “exercise jurisdiction and regulatory authority over the Parking and Barge Operations.” Sub 21 Order, 17, 27.

In reaching this conclusion, the Commission reviewed the history of requests for the Commission to regulate Parking and Barge Operations. In discussing the request for the Commission to regulate the Parking and Barge Operations in the Ferry’s 2010 rate case in Docket No. A-21, Sub 7 (Sub 7), the Commission noted that “[i]t was only because the parties reached a workable solution that was satisfactory to all — to include certain rate, and other, concessions of both BHIL and BHIT as set out above — that the issue was not reached at that time.” Sub 21 Order, 13. Part of the “workable solution” was the imputation of parking revenue in the Commission-approved settlement in Sub 7.

III. General Rule: Net Book Value Rate Base

By statute, the rate base of public utilities in North Carolina is set at the “reasonable original cost . . . of the public utility’s property.”³ Specifically, N.C.G.S. § 62-133 provides, in part, as follows:

- (a) In fixing the rates for any public utility . . . the Commission shall fix such rates as shall be fair both to the public utilities and to the consumer.
- (b) In fixing such rates, the Commission shall:
 - (1) Ascertain the reasonable original cost . . . of the public utility's property used and useful, or to be used and useful within a reasonable time after the test period, in providing the service rendered to the public within the State, less that portion of the cost that has been consumed by previous use recovered by depreciation expense.
- (d) The Commission shall consider all other material facts of record that will enable it to determine what are reasonable and just rates

As Applicants’ witness Taylor confirms, the Commission has “generally ruled that rate base will be the lesser of net original cost or the purchase price when a utility acquisition is made.” Tr. vol. 7, 94. In this proceeding, there is no request for any Acquisition Adjustment for the Ferry and Tram Operations. The Applicants argue, however, that it is appropriate to use the purchase price of the Parking and Barge Operations as the amount that should be included in rate base under the premise that the Parking and Barge Operations are a “newly regulated” utility or, in the alternative, that an Acquisition Adjustment for Parking and Barge

³ N.C.G.S. § 62-133(a)(1).

Operations should be allowed under the special facts and circumstances of this case. Tr. vol. 7, 95-100, Tr. vol. 8, 29-30.

As such, the ultimate issue is whether any portion of the purchase price for Parking and Barge Operations in excess of the net book value should be allowed into rate base, and if so, to what extent.⁴

IV. Only the Net Book Value of the Parking and Barge Operations Should Be Included in Rate Base

In its Order Approving Transfer and Denying Acquisition Adjustment issued on January 6, 2000, in Docket No. W-1000, Sub 5 (North Topsail Order) (citing to a 1990 Carolina Water general rate case), the Commission addressed the regulatory status of a utility's assets and its impact on the value to be included in rate base:

[a]s a general proposition, when a public utility buys assets that have previously been dedicated to public service as utility property, the acquiring utility is entitled to include in rate base the lesser of the purchase price or the net original cost of the acquired facilities in the hands of the transferor at the time of the transfer." In re Carolina Water Service, Inc., of North Carolina. Docket No. W-354, Subs 74, 79, 81, Eightieth Report of the North Carolina Utilities Commission: Orders and Decisions 342, 394 (1990) (Carolina Water II)

North Topsail Order, 24.

⁴ The net book values of the Parking Operation and Barge Operation as presented by the Village are, respectively, **[BEGIN CONFIDENTIAL]** [REDACTED]. **[END CONFIDENTIAL]** Tr. Exhibits vol. 4, O'Donnell Exhibit 2 (Affidavit of Julie Perry, 2), an excerpt of which is attached hereto as Exhibit 1. See also Tr. Exhibits vol. 7, BHIT Public Staff Cross Exhibits 1 and 2 (Taylor Calculations of Rate Impact – Parking and Barge).

Applicants' witness Taylor argues that the original cost to the Applicants in this case is the purchase price because the "parking and barge assets have not been owned by a utility and have not been regulated assets." Tr. vol. 7, 95. Witness Taylor indicates that the Commission should set rate base at "the lesser of purchase price or fair market value for the parking and barge assets - which, in this case, the purchase price is the fair market value." *Id.* In his testimony summary, witness Taylor indicated that setting rate base for the Parking and Barge Operations at the purchase price was a "matter of fundamental regulatory economics, the correct outcome in this unique circumstance, . . . so that the returns on the investment will be sufficient to attract necessary capital, and in this case, doing so will not adversely affect the current rates paid by ratepayers." Tr. vol. 7, 113. Applicants' witness Taylor created his own version of Village witness Perry's exhibit to her affidavit (Tr. vol. 4 Exhibits, Exhibit KWO-6, 5-6), depicting a scenario in which the entire purchase price is placed into rate base. Witness Taylor's table is attached hereto as Exhibit 2.

Contrary to Applicants' witness Taylor's assertions, the Parking and Barge Operations were not, by virtue of the Sub 21 Order, transformed from unregulated to regulated assets, rather the Commission recognized their status as part of the regulated utility and determined that the Parking and Barge Operations could "continue to operate under their existing rates, terms, and conditions, each as an ancillary service covered under BHIT's certificate of public convenience and necessity (CPCN), and under BHIT's current reporting obligations". Sub 21 Order, 28. Of course, as the Parking and Barge Operations are regulated assets pursuant

to the Sub 21 Order, the transferee will be acquiring regulated assets from the transferor in this proceeding. Further, even under the Applicants' argument that the Parking and Barge Operations only recently became regulated, N.C.G.S. § 62-133 does not make a distinction between longstanding or recently designated utility assets in determining "original cost."

This result is also supported by policy concerns. As Village witness O'Donnell pointed out, allowing buyers to place assets into rate based at fair market value – rather than book value – would mean that "ratepayers will have to *pay again* for assets for which they have already paid. Ratepayers should not be forced to pay twice for a utility asset." Tr. vol. 4, 178.

In short, the facts in this case and public policy support a decision that the net original cost of the Parking and Barge Operations should be determined in the usual manner by using the original cost of the assets minus their depreciation.

V. General Rule: No Acquisition Adjustments

The Commission generally has not allowed a positive purchase price acquisition adjustment except when it finds: 1) the benefit to customers outweighs the cost of inclusion in rate base of the excess purchase price; 2) the transaction is prudent; 3) the transaction is the result of arm's length bargaining. (See Order Approving Transfer, Acquisition Adjustment, and Maintaining Current Rates, Docket No. W-274, Sub 122, April 30, 1997 (the Hardscrabble Order), Finding of Fact No. 14.) Further, in the North Topsail Order the Commission stated:

After noting that requests for rate base treatment of acquisition adjustments should be dealt with on a case by-case basis, the Hearing Examiner opined that "the benefits of the acquisition to the acquired customers and to existing customers [may] merit the inclusion of the debit acquisition adjustment" in rate base in some instances. Carolina Water I 739, 756 (1986).

North Topsail Order, 23.

In its North Topsail Order, the Commission adopted a general rule prohibiting the inclusion of Acquisition Adjustments,⁵ though found that many factors can be considered in determining whether "special circumstances" exist to support an Acquisition Adjustment, with two core underlying tests and all relevant facts being considered:

Assuming the appropriateness of adopting a general rule prohibiting the inclusion of acquisition adjustments in rate base in the absence of a showing of special circumstances justifying a contrary decision, the next question becomes one of identifying the circumstances under which rate base treatment of acquisition adjustments should be deemed proper. As should be apparent from an analysis of the Commission's previous Orders concerning this subject, a wide range of factors have been considered relevant in attempting to resolve this question, including the prudence of the purchase price paid by the acquiring utility; the extent to which the size of the acquisition adjustment resulted from an arm's length transaction; the extent to which the selling utility is financially or operationally "troubled;" the

⁵ In adopting this general rule in its North Topsail Order, the Commission looked to how jurisdictions across the country have addressed the appropriateness of acquisition adjustments:

A majority of regulatory agencies in the United States have decided that all other things being equal, acquisition adjustments should not be afforded rate base treatment. According to [the] Bonbright [treatise], "most commissions are skeptical of transfers between utilities at excess costs, so rate base adjustments are generally not made unless the utility can demonstrate actual, distinct and substantial benefits to all affected ratepayers." The adoption of such a general rule is clearly appropriate, for the routine inclusion of acquisition adjustments in rate base would tend to create an incentive for purchasers to pay a high price to acquire utility assets, confident in the knowledge that such payments would be recouped from ratepayers.

North Topsail Order, at 26.

extent to which the purchase will facilitate system improvements; the size of the acquisition adjustment; the impact of including the acquisition adjustment in rate base on the rates paid by customers of the acquired and acquiring utilities; the desirability of transferring small systems to professional operators; and a wide range of other factors, none of which have been deemed universally dispositive. Although the number of relevant considerations seems virtually unlimited, all of them apparently relate to the question of whether the acquiring utility paid too much for the acquired utility and whether the customers of both the acquired and acquiring utilities are better off after the transfer than they were before that time. This method of analysis is consistent with sound regulatory policy since it focuses on the two truly relevant questions which ought to be considered in any analysis of acquisition adjustment issues. It is also consistent with the construction of G.S. 62-111 (a) adopted in *State ex rel. Utilities Commission v. Village of Pinehurst*. 99 N.C. App. 224, 393 S.E.2d 111 (1990), *affd* 331 N.C. 278, 415 S.E.2d 199 (1992), which seems to indicate that all relevant factors must be considered in analyzing the appropriateness of utility transfer applications. As a result, contrary to the approaches advocated by both UI and the Public Staff, the Commission should refrain from allowing rate base treatment of an acquisition adjustment unless the purchasing utility establishes, by the greater weight of the evidence, that the price the purchaser agreed to pay for the acquired utility was prudent and that both the existing customers of the acquiring utility and the customers of the acquired utility would be better off [or at least no worse off] with the proposed transfer, including rate base treatment of any acquisition adjustment, than would otherwise be the case.

North Topsail Order, 27.

VI. Consideration of Factors as to Appropriateness of an Acquisition

Adjustment

Beyond the Commission's general prohibition on Acquisition Adjustments, there are a number of reasons why a **[BEGIN CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** (Tr. vol. 7, 113) Acquisition Adjustment would not be warranted in this case, including: 1) this not a troubled system; 2) this is not fully an arm's

length transaction; 3) the utility does not have ownership or control of the property necessary to operate the Parking and Barge Operations; 4) the final allocation of the purchase price will not be determined until closing; and 5) the parties' Asset Purchase Agreement (APA) includes features that make an evaluation of the reasonableness of the purchase price difficult if not impossible, potential inflation of the overall purchase price, and other incentives such as [BEGIN CONFIDENTIAL] [REDACTED]

[REDACTED]⁶ [END CONFIDENTIAL]

The Utility is Not Troubled

The Bald Head Island ferry, tram, barge, and parking operations are clearly not troubled. It is well known and documented that the Mitchell family has extraordinary financial resources. Mr. Mitchell was one of the wealthiest Americans,⁷ but the Mitchell Estate has decided to sell this operating business as part of winding down the Estate. Should the Transfer Application be denied or the Proposed Transaction fall through, there is no evidence that the utility would not have the means to continue to operate reliably and provide satisfactory service. Further, while unlikely, should the current owners refuse to continue to operate the utility or provide inadequate service, the Commission has statutory tools to protect

⁶ In this instance, and depending upon the term and other provisions of a ground lease, a long-term lease would be a reasonable means of obtaining ownership or control of the property on which the utility will operate; beyond evaluation of market rates and affiliate costs, such leases can be viewed as an alternative to and, among other things, compared against the costs (and benefits) of acquiring the property and related financing.

⁷ Tr. vol. 2, 57, Tr. vol. 5, 157.

the customers, including conducting an investigation, assessing fines, or appointing an emergency operator. See Tr. vol. 6, 69-70; N.C.G.S. §§ 62-37, 73, 262(k), and 310. The fact that the current owners have a strong desire to sell the utility does not make this utility a troubled system. While there was evidence from customers of a marginal decline in the quality of service during the time that the Estate has been pursuing a sale as described by Village witness Gardner (Tr. vol. 4, 81-85), the Public Staff witnesses indicated that they had not identified deficiencies in the management, deficiencies in the operations (though they did identify opportunities for improvements), or financial deficiencies. Tr. vol. 6, 201-02. The Buyers have indicated that they are “willing and able to provide the operations with the capital they need to accommodate growth and enhance the passenger experience while maintaining cost-effective and efficient operations.” Tr. vol. 3, 17.

The Transaction is Not Fully at Arm’s Length

The proposed transaction is between a number of parties or entities, but one of the principals, Mr. Charles A. Paul, III, would be on both sides of the transaction. Mr. Paul presently serves as President of BHIT and CEO and Manager of BHIL, BHIT's parent company. Tr. vol. 2, 33. Upon closing, in addition to retaining an operational role with the new organization, Mr. Paul will serve as a Manager (along with Lee H. Roberts and Douglas A. Vaughn) on the Board of Managers of SVC Pelican Partners, LLC (Partners), the manager of Holdings and therefore, BHIFT. Tr. vol. 9, 138, Tr. vol. 6, 137. By virtue of the prospective

management agreement among Partners, Holdings, and SharpVue, SharpVue would step into the shoes of Partners as manager of Holdings. Tr. vol. 6, 137. Thus, the transaction would not be fully at arm's length when a principal is participating on both sides.

The Utility Lacks Ownership or Control

Further complicating any determination of rate base is the fact that the proposed Buyers of the Parking and Barge Operations have not memorialized the ground leases or other means by which they will have ownership or control over the land on which they intend to operate post-closing. Public Staff witness Boswell, in response to a question regarding whether unowned assets can be included in rate base, indicated that doing so would require "a lease or some kind of an agreement that gave them control or ownership of the asset." Tr. vol. 6, 244.

[BEGIN CONFIDENTIAL] [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] **[END CONFIDENTIAL]** Tr. vol. 3, 34-36. As such, until there are leases for the parking and barge approved by the Commission, it would be virtually impossible to utilize anything other than net book value for inclusion in rate base.

The Allocation of the Purchase Price Has Not Been Finalized

In this proceeding, there are only “preliminary estimated” allocations of the purchase price associated with these operations, allocations that are **[BEGIN CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** Tr. vol. 4, 59.

[BEGIN CONFIDENTIAL]

[REDACTED] [END CONFIDENTIAL] Tr. vol. 9, 20. As Public Staff witness Boswell explained, “[y]ou don’t have a set allocation of the purchase price” and “estimates in accounting world don’t sit so well. So until you have those things set, it’s really hard to determine what the purchase price is, and what, if any, acquisition adjustment should be.” Tr. vol. 6, 245, 250. As such, any discussion of an Acquisition Adjustment is premature until the allocation is final, and then it would be subject to a determination of whether it was reasonable.

The Overall Transaction Structure Makes It Difficult, If Not Impossible, to
Evaluate the Reasonableness of the Purchase Price

Applicants point to a recent lender-obtained appraisal to justify the prudence of the purchase price. Tr. vol. 6, 117, Tr. vol 9, 25-26. However, the higher purchase price is in part a function of, and clouded by, the overall transaction structure as set out in the Asset Purchase Agreement, in particular, **[BEGIN**

CONFIDENTIAL] [REDACTED]

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[REDACTED] [END CONFIDENTIAL]

**VII. The Benefits of the Transfer Outweigh the Costs if the Original
Net Cost Is Included in Rate Case and No Acquisition Adjustment is
Allowed**

The Settlement Agreement and Stipulation with Regulatory Conditions serve to ensure that customers should not be negatively impacted by the Transfer. Further, there is the prospect of additional investment by the new owners to the benefit of customers, though the details of any ground leases and any possible rate base determination remain for future consideration. In this regard, the Commission should weigh, *inter alia*, the Seller's reluctance to continue to operate and provide capital to the ferry, tram, barge, and parking operations against the Buyer's willingness to buy and ability to operate these businesses; the Buyer's reliance on the operational expertise and continuity of existing utility operations managers Paul, Mayfield, and Stewart; and the Buyer's access to capital to continue operations. However, a reassessment of this cost-benefit analysis would

be required should the Commission determine that the purchase price should be considered the original cost or should an Acquisition Adjustment be allowed. In either of these cases, the rates for the ferry, tram, barge, or parking could be increased to such an extent that these additional costs could outweigh the benefits listed above. Of course, the relevant information is not yet available to allow proper evaluation of the impact of allowing the purchase price to be included in rate base or any Acquisition Adjustment.

WHEREFORE, the Public Staff prays:

1. That the Commission find that a determination of the rate base of the utility is not necessary for consummation of the Transfer;
2. That, in the alternative, should the Commission find a rate base determination necessary at this time, the Commission find that the rate base is the original cost less depreciation, being **[BEGIN CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** for the Parking Operations, and **[BEGIN CONFIDENTIAL]** [REDACTED] **[END CONFIDENTIAL]** for the Barge Operations;
3. That, should the Commission deem it appropriate to consider whether an Acquisition Premium should be allowed, the Commission consider and weigh the factors as outlined by the Public Staff and find that a request for an Acquisition Adjustment should be denied; and
4. For such other and further relief as the Commission may deem just and proper.

Respectfully submitted this the 22nd day of May 2022.

PUBLIC STAFF

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Electronically submitted
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CERTIFICATE OF SERVICE

I certify that a copy of these Initial Comments has been served on all parties of record or their attorneys, or both, by United States mail, first class or better; by hand delivery; or by means of facsimile or electronic delivery upon agreement of the receiving party.

This the 22nd day of May 2023.

Electronically submitted

/s/ William E. H. Creech

PUBLIC STAFF EXHIBIT 1

PUBLIC STAFF EXHIBIT 2

PUBLIC STAFF EXHIBIT 3