BEFORE THE

NORTH CAROLINA UTILITIES COMMISSION

PUBLIC SERVICE COMPANY OF NORTH CAROLINA, INC.

DOCKET NO. G-5, SUB 632
DOCKET NO. G-5, SUB 634

REBUTTAL TESTIMONY

OF

MICHAEL B. PHIBBS

OCTOBER 7, 2021

Q. PLEASE STATE YOUR NAME, POSITION, BUSINESS ADDRESS AND PROFESSIONAL BACKGROUND.

A. My name is Michael B. Phibbs, and my business address is 120 Tredegar Street, Richmond, Virginia 23219. I am General Manager – Financial and Business Services. I am employed by Dominion Energy Services, Inc. When I filed my direct testimony, I was employed as Director – Corporate Finance and Assistant Treasurer for Dominion Energy, Inc. ("DEI") and subsidiaries including Public Service Company of North Carolina, Inc. ("PSNC" or the "Company"). On September 1, 2021, I assumed my new position.

Q. ARE YOU THE SAME MICHAEL PHIBBS WHO PROVIDED DIRECT TESTIMONY IN THIS PROCEEDING?

A. Yes.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS PROCEEDING?

A. The purpose of my rebuttal testimony is to respond to the testimony of Public Staff witness John R. Hinton and Carolina Utility Customers Association witness Kevin W. O'Donnell regarding the Company's proposed capital structure and to Mr. Hinton's testimony regarding cost of debt. On proposed capital structure, I will primarily address Mr. Hinton's assertions that the Company is earning excessive returns not required to maintain credit ratings and his and Mr. O'Donnell's use of hypothetical capital structures.

Q. WHAT IS THE CAPITAL STRUCTURE THAT THE COMPANY PROPOSES TO USE IN THIS PROCEEDING?

A. The Company's original filing proposed 43.79% long-term debt, 1.33% short-term debt, and 54.88% common equity, based on PSNC's projected capital structure as of June 30, 2021. In its supplemental filing on August 10, 2021, the Company proposed a capital structure of 43.80% long-term debt, 1.34% short-term debt, and 54.86% common equity, based on the actual capital structure as of June 30, 2021. While both Mr. Hinton and Mr. O'Donnell addressed the original proposed 54.88% common equity ratio, my rebuttal testimony assumes that their opinions would be the same for a common equity ratio of 54.86%. Likewise, the statements I made in my direct testimony supporting the Company's need for 54.88% common equity apply to a common equity of 54.86%.

Q. MR. HINTON DESCRIBES THE COMPANY'S PROPOSED COMMON EQUITY RATIO AS EXCESSIVE. DO YOU AGREE?

A. No, I do not. As explained in my direct testimony, the proposed common equity ratio balances the Company's financing needs to fund operations to meet its service obligations and to achieve credit rating objectives that enable efficient access to capital at reasonable terms.

Q. WHAT IS THE PRIMARY BASIS FOR MR. HINTON'S ASSERTION THAT THE COMPANY IS EARNING EXCESSIVE RETURNS AT A 54.88% COMMON EQUITY RATIO?

A. Generally, Mr. Hinton argues that the Company does not require a common equity ratio of 54.88% in order to maintain its current credit ratings by referencing financial metric data from Moody's Investment Services ("Moody's").

Q. HOW DOES MR. HINTON DESCRIBE WHAT IS NECESSARY TO MAINTAIN THE COMPANY'S CURRENT CREDIT RATINGS?

A. Mr. Hinton selectively highlights certain Moody's financial metrics, namely Cash Flow Operations (pre-working capital)/Debt ("CFO pre-WC/debt"), in making his argument. He asserts that, because the financial metric has been above and below 15%, the Company does not require the 54.88% common equity ratio.

Q. DO YOU AGREE WITH MR. HINTON'S ASSERTION?

A. I do not. Mr. Hinton ignores that Moody's has stated in published reports that the Company would be at risk of a downgrade if the CFO pre-WC/debt financial metric "remains below 15%", which it has been for the past three years. Therefore, 15% is the minimum requirement, and values above that figure are indicative of what is required to maintain PSNC's current rating.

Mr. Hinton shows year-ending data for 2017-2020 and a last twelve-month view based on March 31, 2021. In 2017, Moody's stated 20.4% metric was during a time in which the Company was rated A3, and Moody's reports suggested 20% was a threshold at which Moody's could reasonably expect to consider a downgrade – an entirely different circumstance that is not relevant to the current status of the Company. See Phibbs Rebuttal Exhibit 1 for a copy of Moody's July 23, 2018 report, which included verbiage pertaining to the 20% threshold.

Subsequent to 2017, the financial credit metric of the Company fell like many others in the industry as the effects of federal tax reform lowered rates to customers and thus cash flow, with the metric reported as Mr. Hinton testifies at 12.1%, 12.6%, and 14.3% for the three consecutive years ending 2018, 2019, and 2020. In January 2020, Moody's downgraded the Company's credit rating from A3 to Baa1 due to the continuance of weakened financial metrics in the 2018-2020 period.

It is important to note that, despite the downgrade, Moody's has praised Dominion Energy's efforts of ensuring balance sheet strength as a "supportive parent" and mentioned that the parent company had "refrained from extracting dividends from the utility" and contributed equity as "a show of parental credit support and conservative financial policies for PSNC." See Phibbs Rebuttal Exhibit 2 for a copy of Moody's February 8, 2021 report. It is on this basis, as well as the expectation of "supportive regulatory treatment" within this general rate case, that the Company believes Moody's did not consider a further downgrade notch, as the expectation would be that the Company would maintain above a 15% financial metric in the future, despite not exhibiting this level from 2018-2020.

I also note that the Mr. Hinton's use of March 31, 2021 financial metric data is selective. The published metric by Moody's is actually 19.7%. See page 1 of Phibbs Rebuttal Exhibit 3. Further, while the last twelve month metrics are an indicator of interim performance, Moody's typically places more weight on year-end metrics to be determinative of credit actions. By using the March 31, 2021 metric in association with all other metrics at respective December 31 year-ends, Mr. Hinton introduces bias to where metrics may not be assessed on an apples-to-apples basis, as items such as regulatory assets and liabilities may ebb and flow throughout the year. This could unduly influence metrics utilizing differing time periods. In fact, as shown on page 2 of Phibbs Rebuttal Exhibit 3, the associated credit ratio for the twelve months ended June 30, 2021, is only 15.1%, which is very close to the minimum threshold to prevent further credit rating degradation, and is not indicative of excessive returns.

To summarize the above points, in order to maintain current credit ratings at Moody's, the Company needs to demonstrate the ability to maintain at least a 15% CFO pre-WC/debt ratio. The Company has not met this metric level at year end in the past three years. With supportive actions that Moody's has noted, as well as the expectation of supportive regulatory treatment, the Company believes it is now on track to do so. Those supportive Company actions, namely infusing equity to balance the capital structure and forgoing dividends through the end of 2020, has resulted in an actual filed capital structure of 54.86%, which the Company believes is necessary and prudent to maintain adequate access to capital, support current credit ratings, and provide a balanced approach to funding the necessary infrastructure to meet its service obligations.

Q. WHAT COMMON EQUITY RATIOS DO MR. HINTON AND MR O'DONNELL RECOMMEND FOR PSNC?

A. Mr. Hinton recommends a common equity ratio of 50.90% for PSNC. He uses a hypothetical capital structure based on the average capital structures approved in general rate cases for LDCs in 2020 and 2021 as reported by Standard and Poor's Capital IQ and shown on Hinton Exhibit 5. I note that Mr. Hinton admitted that he had departed from his usual practice of recommending a capital structure based on a 13-month historical average, which would have resulted in using a common equity ratio of 53.65% as shown on Hinton Exhibit 4. Mr. Hinton offered no explanation for this departure.

Mr. O'Donnell uses a 50% hypothetical common equity ratio in his testimony.

Q. IN YOUR VIEW IS THE USE OF A HYPOTHETICAL CAPITAL STRUCTURE TYPICAL?

A. No, it is not. As Company witness Nelson testifies, the filed capital structure of 54.86% is within the range of prudent capital structures approved in other peer utility cases, and most reflective of our current financial position. Mr. Hinton himself describes that typically he would recommend a 13-month average common equity ratio, or an actual 53.65% common equity ratio in this preceding. Using a hypothetical capital structure, or one based simply on what was approved previously emanating from time periods which may not have similar facts and circumstances as the current period, would create inconsistencies between how a Company is actually funded versus the capital on which it may earn.

Q. WHAT IS YOUR OPINION OF USING A 13-MONTH AVERAGE CAPITAL STRUCTURE, WHICH MR. HINTON DESCRIBES AS HIS TYPICAL RECOMMENDATION?

A. It would be most prudent to reflect the actual capital structure at the time of the rate case preceding, which is most reflective of the Company's capital mix. However, a 13-month average capital structure at least is based on the actual financial position of the Company and also reflects relatively recent data. Therefore, I would view that methodology as one that is grounded in sound logic as compared to a hypothetical or "last approved" methodology.

Q. WHAT DO YOU BELIEVE THE EFFECT WOULD BE OF ALLOWING MR. HINTON'S IMPUTED COMMON EQUITY RATIO OF 50.90%, OR MR. O'DONNELL'S 50% IMPUTED CAPITAL RATIO?

A. Imputation of a capital structure would be arbitrary and present significant financial harm to the Company.

My testimony already details that in the past three years, the Company has not maintained necessary financial metrics to secure its credit rating and has experienced a downgrade during a time when its base rates were authorized with a 52% common equity ratio. Mr. Hinton appears to agree that it is in the Company's best interests to maintain its current credit rating, as he looks to triangulate equity ratios that would be supportive of this rating within his testimony. Actions undertaken to solidify the Company's credit standing, which Moody's has viewed favorably, have resulted in a higher common equity ratio than 52%. If the Company could not earn on this prudent and supportive capital structure, and in fact be forced to earn below prior common equity figures despite an increase in the actual common equity ratio, it would send a negative signal to investors and credit agencies alike that North Carolina is not providing "supportive regulatory treatment." A supportive regulatory environment generally entails earning fair returns on a reasonable capital structure. Adopting either of these imputed capital structures would leave the Company with significant equity capital which it cannot earn a return on, could jeopardize current credit ratings, and would not recognize the actions the Company has taken to solidify its balance sheet and ratings since the Company's change in ownership. In addition, Mr. Hinton's approach would harm the Company should that same balance sheet and ratings be deemed inadequate by credit agencies in the form of imposing replacement cost of debt imputations, which he also advocates in his testimony.

Q. WHAT IS PSNC'S CURRENTLY AUTHORIZED COMMON EQUITY RATIO?

A. PSNC's current rates are based on a Commission approved common equity capitalization ratio of 52%.

Q. WHAT DO YOU BELIEVE THE COMMISSION SHOULD DO REGARDING THE COMMON EQUITY RATIO?

A. I believe the Commission should accept the 54.86% common equity ratio included in the Company's supplemental filing, as that represents the most updated view of the Company's balance sheet. That said, any exploration of alternatives to the 54.86% actual common equity ratio must be grounded in recent actual data of the Company, such as a 13-month average view. Certainly, the Commission should not embrace Mr. Hinton's and Mr. O'Donnell's proposals to deteriorate the Company's financial position below its current authorized equity capitalization ratio of 52%.

Q. DO YOU AGREE WITH MR. HINTON'S IMPUTATION OF A COST OF DEBT OF 4.45% DUE TO THE CREDIT DOWNGRADE OF THE COMPANY BY MOODY'S?

A. I do not. Mr. Hinton rightly acknowledges, as does the Company, that a condition of the Dominion Energy, Inc. and SCANA merger was that in the event of a credit rating downgrade, PSNC customers should be held harmless, and a replacement cost of debt utilized if customers are harmed by a resulting higher cost of debt on subsequent issuances. However, Mr. Hinton does not provide any Company-specific facts to support his assertion that the Company's cost of debt was harmed – he merely utilizes bulk average data in the form of Mergent Inc.'s research, as well as his previous investigations into another utility that was downgraded.

In response to a Public Staff data request, the Company explained that there was no pricing degradation in debt issuances after the January 2020 Moody's downgrade. This response provided data showing that the National Association of Insurance Commissioners rating of PSNC did not change, which directly impacts most private debt investors' cost of capital. The data also showed quantitatively that the most recent PSNC debt issuance in 2021 priced better on a credit spread basis relative to the investment grade utility index than any issuance since 2016, well before the downgrade. Mr. Hinton does not offer any specific data to support his conclusion; rather he found the Company's view "unpersuasive."

Q. WHAT DO YOU PROPOSE THE COMMISSION DO REGARDING THE LONG-TERM DEBT RATE?

A. I encourage the Commission to consider that the data specific to PSNC in this particular case shows no harm to ratepayers from the January 2020 Moody's downgrade. I recommend that the Commission accept the 4.48% cost of long-term debt proposed by the Company, which is lower than the embedded cost of long-term debt in the Company's original application due to the 2021 refinancing.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes, it does, although I reserve the right to supplement or amend my testimony before or during the Commission's hearing in this proceeding.

MOODY'S
INVESTORS SERVICE

CREDIT OPINION
23 July 2018

Update

Rate this Research

RATINGS

Public Service Co. of North Carolina, Inc.

Domicile	Gastonia, North Carolina, United States
Long Term Rating	A3
Type	Senior Unsecured - Dom Curr
Outlook	Negative

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Contacts

Laura Schumacher +1.212.553.3853
VP-Sr Credit Officer
laura.schumacher@moodys.com

Dexter East +1.212.553.3260
Associate Analyst
dexter.east@moodys.com

Michael G. Haggarty +1.212.553.7172
Associate Managing Director
michael.haggarty@moodys.com

Jim Hempstead +1.212.553.4318
MD-Utilities
james.hempstead@moodys.com

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

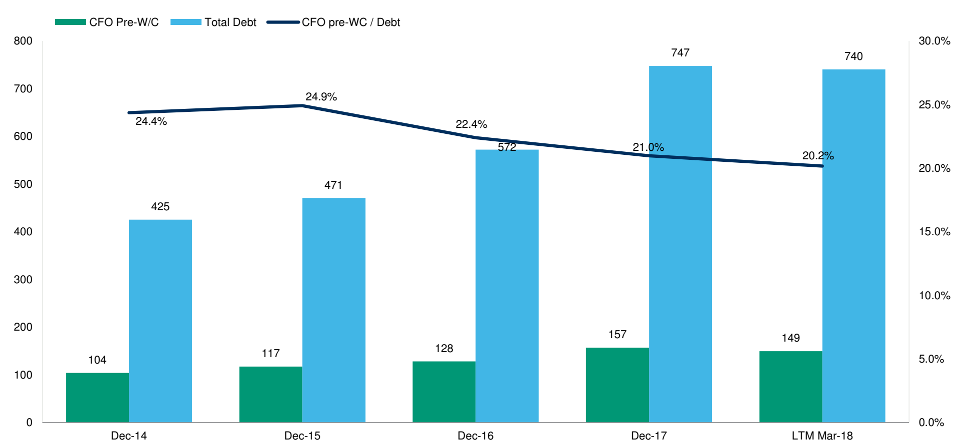
Public Service Co. of North Carolina, Inc.

Update following ratings confirmation

Summary

Public Service Company of North Carolina's (PSNC) credit reflects a supportive regulatory environment, a strong suite of timely cost recovery mechanisms and a low business risk profile. PSNC's gas distribution operations provide stable and predictable financial metrics, which have historically been very strong. Going forward, as the utility ramps up its capital investment, we expect the ratio of cash flow excluding changes in working capital (CFO pre-WC) to debt to decline to around 20%, but to remain supportive of the utility's credit quality. The negative outlook reflects contagion risk associated with its position within the SCANA Corporation (SCANA, Ba1 negative) family, which is facing significant political and regulatory backlash in the wake of PSNC's affiliate, South Carolina Electric & Gas' (SCE&G, Baa3 negative), decision to cease construction of a large nuclear project.

Exhibit 1
Historical CFO Pre-WC, Total Debt and CFO Pre-WC to Debt [1]
($ MM)



[1] CFO Pre-WC is defined as cash flow from operations excluding changes in working capital.
Source: Moody's Financial Metrics

Credit strengths

» Historically supportive regulatory environment and low business risk provide stable and predictable cash flows

» Financial metrics appropriate for the credit

Credit challenges

» Contagion risk derived from its position within the SCANA family

» Heightened political and regulatory risk following SCANA's decision to abandon nuclear construction

» Elevated capital program to provide for growth and distribution system integrity

Rating outlook

PSNC's outlook is negative, recognizing the utility 's position within the SCANA family and the absence of strong ring fencing type provisions that could serve to insulate it from potential financial distress at the parent. As such, and in light of the wide rating differential between PSNC and its parent SCANA, a downward movement in the ratings of SCE&G and SCANA would likely put downward pressure on PSNC.

Factors that could lead to an upgrade

» The rating outlook is negative, as such, the ratings are not likely to move upward over the next 12-18 months

» The outlook could be returned to stable if the open docket at the Public Service Commission of South Carolina (SCPSC) relating to SCE&G results in a rate plan that will support stable and predictable cash flow metrics at SCE&G

» Longer term, upward rating pressure could result if CFO pre-W/C to debt metrics at PSNC were to improve consistently to above 27%, and if there is an upgrade of SCANA

Factors that could lead to a downgrade

» A downgrade of SCE&G and SCANA would likely result in a downgrade of PSNC

» If the North Carolina regulatory environment were to become less credit supportive

» If PSNC's CFO pre-WC to debt falls below 20% for an extended period of time

Key indicators

Exhibit 2

KEY INDICATORS [1]

Public Service Co. of North Carolina, Inc.

	Dec-14	Dec-15	Dec-16	Dec-17	LTM Mar-18
CFO pre-WC + Interest / Interest	5.2x	5.8x	5.8x	5.8x	5.3x
CFO pre-WC / Debt	24.4%	24.9%	22.4%	21.0%	20.2%
CFO pre-WC – Dividends / Debt	16.9%	17.9%	16.5%	16.2%	14.6%
Debt / Capitalization	30.8%	32.0%	34.9%	43.3%	42.0%

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
Source: Moody's Financial Metrics

Profile

Public Service Company of North Carolina (PSNC, A3 negative), a wholly owned subsidiary of SCANA Corporation (SCANA, Ba1 negative), is fully regulated by the North Carolina Utilities Commission (NCUC). PSNC is a local gas distribution utility (LDC) serving approximately 550,000 residential, commercial and industrial customers with a service area of about 12,000 square miles in the state of North Carolina.

Detailed credit considerations

Exposure to affiliate risk

While PSNC's operations have a low business risk profile, its parent SCANA has been exposed to increased business risk due to the construction of the V.C. Summer nuclear plant at its largest subsidiary, SCE&G. With the March 2017 bankruptcy of the project's contractor, SCE&G was exposed to open ended price and construction risk, and in July 2017 announced its decision to abandon the project. We initially viewed this decision as credit positive since it ended the company's exposure to complex construction and cost overrun risk. However, the abandonment decision, and the company's attempts to seek recovery under the state's Base Load Review Act (BLRA), led to an intense public outcry, and an increase in political and regulatory risk that has eclipsed the elimination of construction and price risk in our analysis.

Most recently, in early July, laws were enacted that mandate a temporary reduction in SCE&G's rates, eliminating all increases the utility has received under the BLRA since 2011. Importantly, the reduction is temporary and the law leaves permanent rate making authority with the SCPSC. However, in the current political environment, we think the SCPSC will be pressured to set rates as low as possible and may look to delay or deny recovery of abandonment costs. As such, SCE&G's credit profile could weaken materially.

PSNC could potentially be tapped as a source of additional support via increased up-streamed dividends or return of capital. On average over 2013-2017, PSNC has paid out about 60% of its net income of about $58 million per year as dividends, exhibiting a conservative financial policy. If PSNC were to dividend 100% of its net income (i.e. an extra $23 million per year), it could conceivably cover SCANA parent level interest expense of about $45 million per year. That said, we believe that SCANA's management values PSNC's good relations with its regulators as well as PSNC's credit ratings, both of which could be jeopardized if financial policy were to materially change. We note that SCANA's June decision to reduce its dividend by 80%, to preserve liquidity and options in light of the ongoing uncertainty in South Carolina, left intact the portion of its dividend generated by its gas operations in South Carolina and from PSNC.

Supportive regulatory environment and low business risk provide stable and predictable cash flows

PSNC's credit profile reflects a supportive regulatory environment in North Carolina. PSNC's gas distribution operations are characterized as low business risk due to its regulated nature, generally manageable capital expenditure program, and mostly residential customer base. PSNC benefits from a suite of cost recovery mechanisms, including Rider D – for recovery of all prudently incurred gas costs including realized and unrealized gains and losses from its hedging activities, and a customer usage tracker (CUT) (decoupling) that allows to PSNC to periodically adjust rates for residential and commercial customers based on average per customer consumption.

In addition, in 2016, the North Carolina Utilities Commission (NCUC) authorized PSNC's implementation of an integrity management rider (Rider E) to track and provide ongoing recovery of capital expenses relating to its transmission and pipeline integrity programs, along with regulatory accounting treatment for related operations and maintenance expenses. In 2017, the NCUC approved two biannual rate increases based on the tracking mechanism. We view the use of trackers and riders as supportive of credit quality as they provide some assurance of recovery and significantly reduce regulatory lag, particularly when capital investment is growing.

In its last base rate order (November 2016), the NCUC authorized a $19 million (4%) revenue increase for PSNC premised on a return on equity (ROE) of 9.7%, a capital structure that includes 52% equity, and a rate base of about $950 million. In March 2016, the company had requested an increase of $41 million (9.7%) based on its previously approved (2008) ROE of 10.6%.

Continued growth in service territory

According to Moody's Economy.com, North Carolina's economy is expanding, in step with the national pace. Although the pace of job creation has slowed from its peak, hiring has been broad based with both good producers and service providers steadily adding to headcounts. Much of PSNC's service territory is concentrated in the Raleigh – Durham region which is situated in North Carolina's "research triangle", viewed as a technology powerhouse that is bolstering North Carolina's expansion. Going forward, North Carolina's growth is expected to remain above average, fueled by tech-related investment and strong demographic trends.

Financial metrics are expected to decline somewhat but remain supportive of the credit

PSNC's financial metrics have historically been very strong. For the twelve months ending March 31, 2018 we calculate PSNC's ratio of CFO pre-WC to debt as 20.2%; as of year-end 2016, the ratio was 21%. The ratio of CFO pre-WC plus interest to interest (interest coverage) during the same two periods was 5.3x and 5.8X respectively. As of March 31, 2018, PSNC generated a three year average CFO pre–WC to debt metric of 23.2% and a three year average interest coverage ratio of 5.6x.

Going forward, we expect PSNC's metrics to weaken somewhat as the utility continues to make investments for growth, system reliability and pipeline integrity. However, due in part to the benefits of Rider E for the recovery of transmission and distribution integrity management program capital, we expect CFO pre–WC to debt will remain above 20%.

Liquidity analysis

PSNC maintains weak but acceptable liquidity despite a material adverse change (MAC) clause for new borrowings in its credit facility. For the last twelve months ended March 31, 2018 , PSNC generated approximately $133 million of cash from operations (CFO), invested about $291 million in capital expenditures, and up streamed $41 million in dividend payments, resulting in negative free cash flow (FCF) of about $199 million. For FY 2017, PSNC generated approximately $106 million of CFO, invested approximately $278 million in capital expenditures and up streamed $36 million in dividend payments to parent SCANA, resulting in negative FCF of approximately $208 million. We expect PSNC to be cash flow negative over the next few years as capital expenditures remain elevated, as the company retrofits its pipeline assets to increase capacity and ensure reliability, and some distributions are paid to the parent.

The utility has a $200 million stand-alone credit facility that expires in December 2020. As of March 31, 2018, there was about $93 million of borrowings outstanding on the facility reducing available capacity to approximately $109 million. The credit facility has a single financial covenant requiring PSNC to maintain a consolidated debt to capitalization ratio of no more than 70%. As of March 31, 2018 PSNC was in compliance with its financial covenant and we estimate the debt to capitalization ratio to be about 45%. The facility also requires a representation that there has not been a material adverse change (MAC) for new borrowings. The MAC requirement is negative for credit as it may preclude borrowing under the facility when it is needed most. PSNC's next long term debt maturity is $100 million of first mortgage bonds due in March of 2020.

Rating methodology and scorecard factors

Exhibit 3

Rating Factors				
Public Service Co. of North Carolina, Inc.				
Regulated Electric and Gas Utilities Industry Grid [1][2]	**Current LTM 3/31/2018**		**Moody's 12-18 Month Forward View As of Date Published [3]**	
Factor 1 : Regulatory Framework (25%)	**Measure**	**Score**	**Measure**	**Score**
a) Legislative and Judicial Underpinnings of the Regulatory Framework	A	A	A	A
b) Consistency and Predictability of Regulation	Aa	Aa	Aa	Aa
Factor 2 : Ability to Recover Costs and Earn Returns (25%)				
a) Timeliness of Recovery of Operating and Capital Costs	A	A	A	A
b) Sufficiency of Rates and Returns	Baa	Baa	Baa	Baa
Factor 3 : Diversification (10%)				
a) Market Position	Ba	Ba	Ba	Ba
b) Generation and Fuel Diversity	N/A	N/A	N/A	N/A
Factor 4 : Financial Strength (40%)				
a) CFO pre-WC + Interest / Interest (3 Year Avg)	5.6x	A	5x - 5.4x	A
b) CFO pre-WC / Debt (3 Year Avg)	23.2%	A	19% - 23%	A
c) CFO pre-WC – Dividends / Debt (3 Year Avg)	17.2%	A	13% - 17%	A
d) Debt / Capitalization (3 Year Avg)	35.2%	Aa	38% - 39%	Aa
Rating:				
Grid-Indicated Rating Before Notching Adjustment		A2		A2
HoldCo Structural Subordination Notching	0	0	0	0
a) Indicated Rating from Grid		A2		A2
b) Actual Rating Assigned		A3		A3

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
[2] As of 3/31/2018(L)
[3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures.
Source: Moody's Financial Metrics

Appendix

Exhibit 4

Peer Comparison Table [1]

	Public Service Co. of North Carolina, Inc. A3 Negative			Piedmont Natural Gas Company, Inc. A2 Negative			DTE Gas Company A2 Negative			Spire Alabama Inc. A2 Stable		
(in US millions)	FYE Dec-16	FYE Dec-17	LTM Mar-18	FYE Dec-16	FYE Dec-17	LTM Mar-18	FYE Dec-16	FYE Dec-17	LTM Mar-18	FYE Sep-16	FYE Sep-17	LTM Mar-18
Revenue	423	470	495	1,149	1,328	1,381	1,308	1,368	1,360	369	401	494
CFO Pre-W/C	164	205	203	398	457	450	390	419	405	159	170	169
Total Debt	572	747	740	2,030	2,511	2,254	1,537	1,784	1,692	422	489	476
CFO pre-WC / Debt	22.4%	21.0%	20.2%	20.7%	18.7%	19.0%	17.2%	17.4%	17.9%	32.7%	30.0%	30.3%
CFO pre-WC – Dividends / Debt	16.5%	16.2%	14.6%	15.1%	18.7%	19.0%	10.9%	11.5%	11.6%	25.3%	24.5%	23.6%
Debt / Capitalization	34.9%	43.3%	42.0%	44.6%	53.3%	49.4%	38.8%	46.4%	44.1%	32.8%	36.1%	36.5%

[1] All figures & ratios calculated using Moody's estimates & standard adjustments. FYE = Financial Year-End. LTM = Last Twelve Months. RUR* = Ratings under Review, where UPG = for upgrade and DNG = for downgrade
Source: Moody's Financial Metrics

Exhibit 5

Cash Flow and Credit Metrics [1]

CF Metrics	Dec-14	Dec-15	Dec-16	Dec-17	LTM Mar-18
As Adjusted					
FFO	**125**	**126**	**152**	**171**	**162**
+/- Other	(22)	(9)	(24)	(14)	(13)
CFO Pre-WC	104	117	128	157	149
+/- ΔWC	2	7	(15)	(53)	(19)
CFO	**105**	**124**	**113**	**103**	**131**
- Div	32	33	34	36	41
- Capex	113	133	171	276	289
FCF	**(39)**	**(41)**	**(92)**	**(208)**	**(199)**
(CFO Pre-W/C) / Debt	24.4%	24.9%	22.4%	21.0%	20.2%
(CFO Pre-W/C - Dividends) / Debt	16.9%	17.9%	16.5%	16.2%	14.6%
FFO / Debt	29.5%	26.8%	26.6%	22.9%	21.9%
RCF / Debt	22.1%	19.8%	20.7%	18.1%	16.4%

[1] All figures and ratios are calculated using Moody's estimates and standard adjustments. Periods are Financial Year-End unless indicated. LTM = Last Twelve Months
Source: Moody's Financial Metrics

Ratings

Exhibit 6

Category	Moody's Rating
PUBLIC SERVICE CO. OF NORTH CAROLINA, INC.	
Outlook	Negative
Sr Unsec Bank Credit Facility	A3
Senior Unsecured	A3
Commercial Paper	P-2
PARENT: SCANA CORPORATION	
Outlook	Negative
Issuer Rating	Ba1
Sr Unsec Bank Credit Facility	Ba1
Senior Unsecured	Ba1
Commercial Paper	NP

Source: Moody's Investors Service

REPORT NUMBER 1133063

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

MOODY'S INVESTORS SERVICE

MOODY'S
INVESTORS SERVICE

CREDIT OPINION
8 February 2021

Update

Rate this Research

RATINGS

Public Service Co. of North Carolina, Inc.

Domicile	Gastonia, North Carolina, United States
Long Term Rating	Baa1
Type	Senior Unsecured - Dom Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Contacts

Ryan Wobbrock +1.212.553.7104
VP-Sr Credit Officer
ryan.wobbrock@moodys.com

Poonam Thakur +1.212.553.4635
Associate Analyst
poonam.thakur@moodys.com

Michael G. Haggarty +1.212.553.7172
Associate Managing Director
michael.haggarty@moodys.com

Jim Hempstead +1.212.553.4318
MD - Global Infrastructure & Cyber Risk
james.hempstead@moodys.com

Public Service Co. of North Carolina, Inc.

Update to credit analysis

Summary

Public Service Company of North Carolina's (PSNC) credit is supported by 1) it's low risk operations as a local gas distribution company (LDC), 2) a generally supportive regulatory environment that provides allowed returns and cost recovery mechanisms in line with industry norms and 3) a Customer Usage Tracker (CUT) and Infrastructure Modernization Tracker (IMT) that enhance the predictability and stability of cash flow amid PSNC's current rate freeze.

PSNC's credit is constrained by the likelihood that weakened financial metrics will remain lower for longer due to 1) increased leverage that has helped fund the utility's capital program, 2) a base rate freeze through November 2021, and 3) the negative cash flow impacts of federal tax reform, once new rates are set in place, which we expect to occur in 2022.

COVID-19 considerations

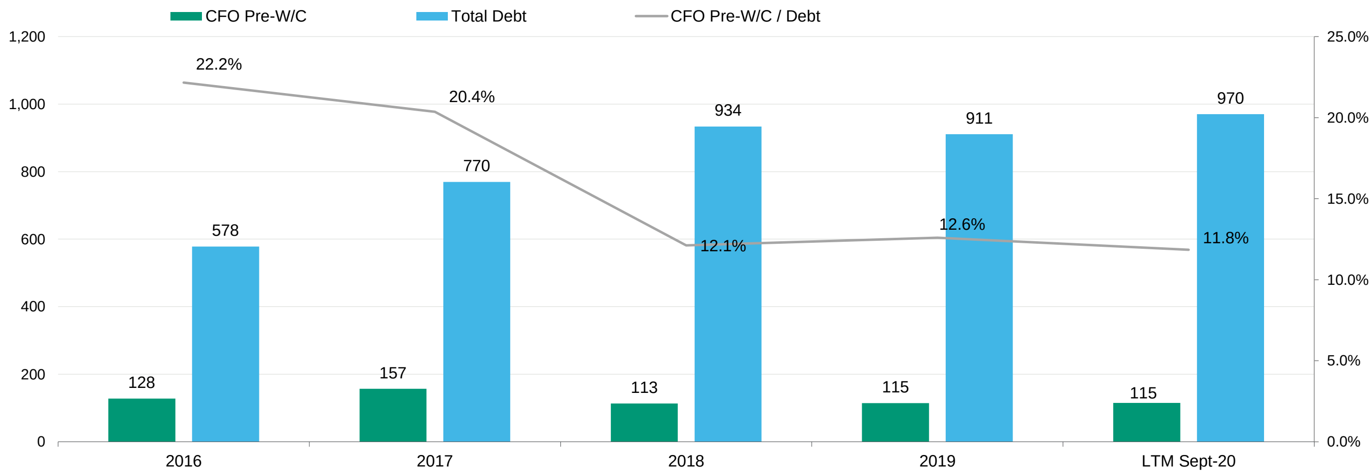
The rapid spread of the coronavirus outbreak, severe global economic shock, low oil prices, and asset price volatility are creating a severe and extensive credit shock across many sectors, regions and markets. The combined credit effects of these developments are unprecedented. We regard the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety.

We expect PSNC to be relatively resilient to recessionary pressures because of its rate regulated operations and cost recovery mechanisms, such as the CUT and IMT and a strong underlying economy in Raleigh, even amid COVID-19 pressures.

Nevertheless, we are watching for natural gas volume declines, utility bill payment delinquency, and the regulatory response to counter these effects on earnings and cash flow. As events related to the coronavirus continue, we are taking into consideration a wider range of potential outcomes, including more severe downside scenarios. The effects of the pandemic could result in financial metrics that are weaker than expected; however, we see these issues as temporary and not reflective of the long-term financial profile or credit quality of PSNC.

Exhibit 1

Historical CFO Pre-WC, Total Debt and CFO Pre-WC to Debt ($ MM)



The downgrade threshold indicated is one of several factors that could lead to a downgrade if the metric is consistently below that level.
Source: Moody's Financial Metrics

Credit strengths

- Low business risk operations in a supportive regulatory environment
- Revenue decoupling mechanism and infrastructure rider provide solid operating and capital cost recovery despite COVID-19 economic impacts
- Supportive parent with robust financial resources

Credit challenges

- Weak credit metrics for the last three years
- Elevated capital program to provide for growth and distribution system integrity
- Cash flow headwinds due to rate freeze and eventual customer credits for tax reform

Rating outlook

PSNC's stable outlook reflects our expectation that its CFO pre-WC to debt ratio will improve to 15-17% beginning in 2022, following a general rate case filing and what we expect to be supportive regulatory treatment from the North Carolina Utilities Commission (NCUC).

Factors that could lead to an upgrade

- Improved regulatory support for cost recovery (e.g., the use of forward test years in rate making)
- CFO pre-WC to debt above 18% on a sustainable basis

Factors that could lead to a downgrade

- If the North Carolina regulatory environment were to become less credit supportive of timely cost and investment recovery
- CFO pre-WC to debt metric remains below 15%

Key indicators

Exhibit 2
Public Service Co. of North Carolina, Inc.

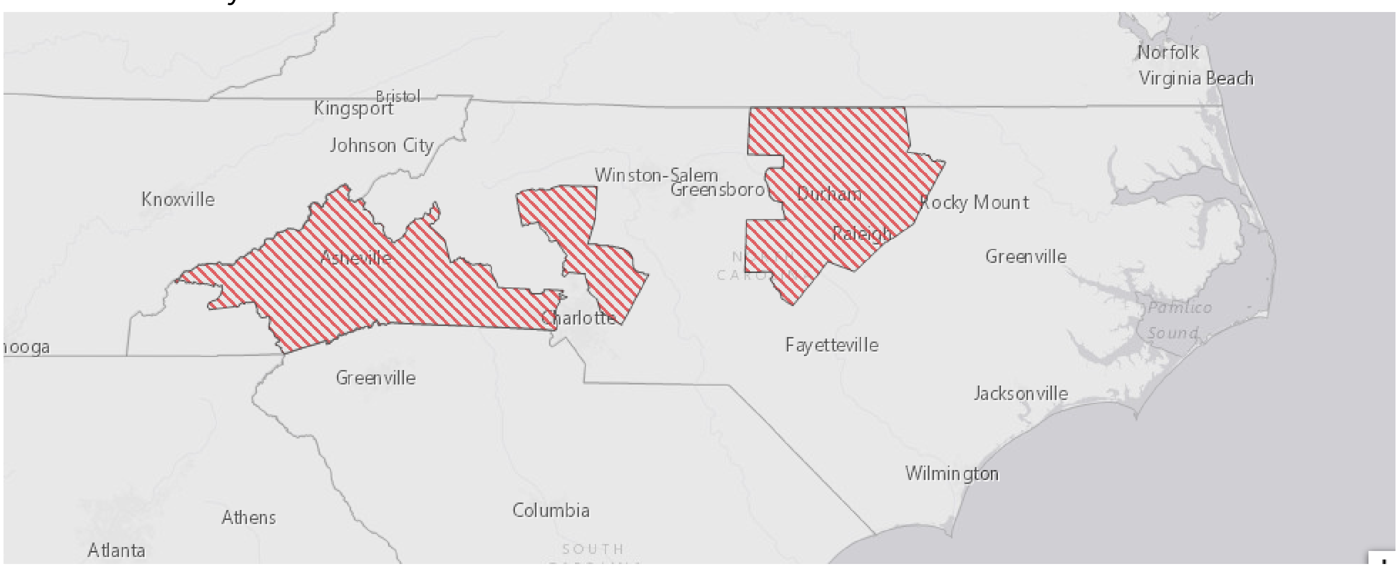
	Dec-16	Dec-17	Dec-18	Dec-19	LTM Sept-20
CFO Pre-W/C + Interest / Interest	6.0x	5.8x	3.7x	3.6x	3.7x
CFO Pre-W/C / Debt	22.2%	20.4%	12.1%	12.6%	11.8%
CFO Pre-W/C – Dividends / Debt	16.3%	15.7%	7.4%	11.2%	11.8%
Debt / Capitalization	35.1%	44.0%	47.2%	43.1%	43.4%

All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
Source: Moody's Financial Metrics

Profile

Public Service Company of North Carolina (PSNC, Baa1 stable), a wholly owned subsidiary of intermediate holding company SCANA Corporation, and ultimate parent company, Dominion Energy, Inc. (Dominion, Baa2 stable), is fully regulated by the North Carolina Utilities Commission (NCUC). PSNC is a local gas distribution utility (LDC) serving approximately 580,000 residential, commercial and industrial customers with a service area of about 12,000 square miles in the state of North Carolina.

Exhibit 3
PSNC's service territory



Source: SPGMI

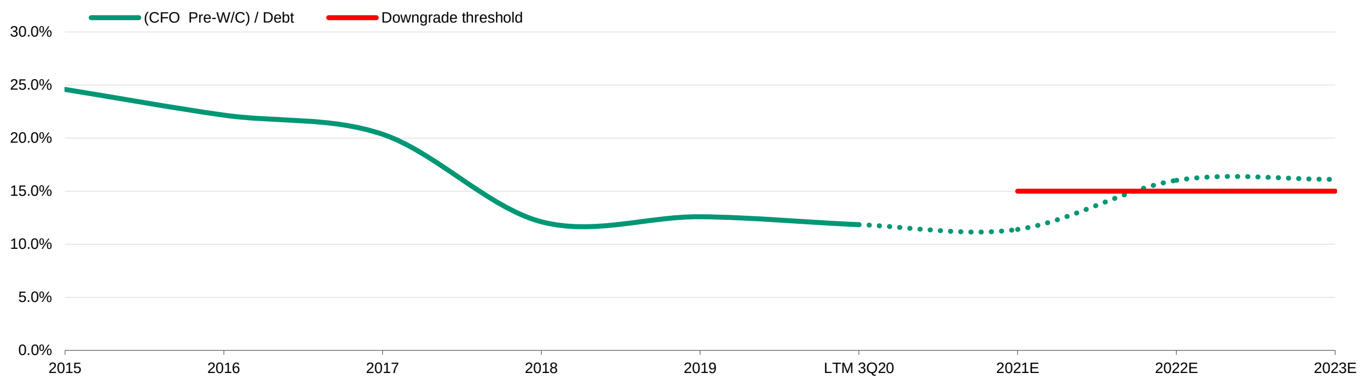
Detailed credit considerations

Weak financial profile should improve with new rate structure in the next 12 months

In November 2018, the NCUC approved the proposed merger of PSNC's parent company SCANA with Dominion. As a condition to the approval order, PSNC agreed to a base rate freeze through November 2021 and to provide customer bill credits of $1.3 million in each of January 2019, 2020 and 2021. As a result, the company's key financial metrics, such as CFO pre-WC to debt, have declined materially over the past 3 years, well below our 15% financial metric threshold identified in the "Factors that could lead to a downgrade" above.

However, during this time, Dominion has refrained from extracting dividends from the utility and contributed $70 million of equity used to repay intercompany borrowings - a show of parental credit support and conservative financial policies for PSNC. Moreover, PSNC's cash flow metrics should improve materially once it is able to implement new rates to recover investments and higher operating costs and capital spending through a general rate case, as seen in the exhibit below. We expect PSNC to exhibit run-rate CFO pre-WC to debt metrics between 15-17% once full rate recovery is in place.

Exhibit 4
PSNC's ratio of CFO pre-WC to debt should recover in 2022, after a full year of higher rates



The downgrade threshold indicated is one of several factors that could lead to a downgrade if the metric is consistently below that level.
Source: Moody's Investors Service

We expect the company to file a rate case soon, given that the rate freeze expires in November 2021. However, the revenue increase associated with the investment recovery will be tempered by cash flow reductions that are commensurate with the December 2017 Tax Cuts and Jobs Act (i.e., loss of bonus depreciation for utilities, federal tax rate reduction to 21% from 35% and the cash return of excess deferred income taxes over a period of time). This will likely keep CFO pre-WC to debt below 18%, even when assuming a supportive general rate case outcome.

We also note that several requests for rate increases across the US have been delayed or mitigated due to economic pressures of the COVID-19 pandemic in 2020. Our base case assumption is that the NCUC will continue to provide adequate and timely recovery of PSNC's costs, as evidenced in roughly $85 million of rate increases allowed in 2020 via the CUT and IMT mechanisms. Should PSNC's rate freeze be extended beyond the November 2021 time frame, the company's financial profile would continue to deteriorate and additional credit pressure could ensue.

Low business risk in a supportive regulatory environment

PSNC's credit profile reflects a supportive regulatory environment in North Carolina. PSNC's gas distribution operations are characterized as low business risk due to their regulated nature, an asset base with no cast iron or bare steel piping and a mostly residential customer base.

PSNC benefits from a suite of cost recovery mechanisms, including Rider D – for recovery of all prudently incurred gas costs including realized and unrealized gains and losses from its hedging activities, and a Customer Usage Tracker (CUT) (decoupling) that allows the PSNC to periodically adjust rates for residential and commercial customers based on average per customer consumption.

Another particularly helpful mechanism is the IMT to track and provide ongoing recovery of capital expenses relating to its transmission and pipeline integrity programs, along with regulatory accounting treatment for related operations and maintenance expenses.
We view the use of trackers and riders as supportive of credit quality as they provide some assurance of recovery and significantly reduce regulatory lag, particularly when capital investment is growing. We note however, that while PSNC is able to recover its capital expenditures for pipeline integrity via rider, its increased operating and maintenance costs are subject to deferral and regulatory lag, which is negatively impacting cash flow.

Both the CUT and IMT have semiannual true-up's which have helped PSNC maintain steady CFO pre-WC amounts of around $115 million per annum from 2018-LTM Q3 2020. The semiannual true-up's have been a positive aspect of regulatory support during 2020 and the accompanying COVID-19 economic pressures, which has been an important qualitative consideration in PSNC's credit profile.

Solid service territory economy, despite COVID challenges

Two of the largest portions of PSNC's service territory are the Raleigh – Durham region and the City of Asheville (Aaa stable), both of which have seen an uptick in unemployment due to COVID-19, but they have credit strengths that should persist longer term to support PSNC"s investment cost recovery.

The City of Raleigh (Aaa stable) is situated in North Carolina's "research triangle", which has several economic strengths despite COVID-19 pressures that have increased Raleigh unemployment to an expected 6.2% rate in 2020, up from 3.4% in 2019, according to Moody's Analytics (MA). MA cites Raleigh's economic strengths, including a low business and living cost environment compared to most other tech hubs, high per capita income that supports consumption, strong and improving migration and a high concentration of prime-age workers - all of which are credit positive features for a utility's service territory.

Ashevlille, on the other hand, has lower wages in public and private sectors and has been hit harder by its dependence on tourism. Asheville's unemployment rate is expected to be around 7.5% in 2020, compared to 3.2% in 2019, according to MA. That said, the city's position as a regional health care hub with favorable migration patterns should continue to support its underlying economic ability to absorb PSNC's rates.

ESG considerations

Environmental

PSNC has low carbon transition risk within the utility sector because it is a gas LDC and natural gas commodity purchase costs are fully passed through to customers with an effective cost recovery mechanism. Moreover, the company's decoupling mechanism helps to insulate its financial profile from the potential negative impacts of lower sales volumes, should usage decline.

However, its primary function is to deliver a fossil fuel for end-use combustion and, accordingly, has methane and ultimately carbon emissions associated with the product. As such, PSNC's business is exposed to longer-term carbon transition risks, especially if state and federal efforts seek to expedite the elimination of greenhouse gas emissions. Dominion is actively addressing its company wide greenhouse gas emissions, with the goal of reaching net zero emissions by 2050, which includes reducing the emission profile of PSNC.

Social

Social risks are primarily related to health and safety, demographic and societal trends, as well as customer relations as the company works to provide reliable and affordable service to customers and safe working conditions to employees.

Regarding affordability, we see the potential for rising social risks associated with the COVID-19 pandemic and its effect on PSNC's service territories to be less than other parts of the US, given Raleigh's economic strengths. However, should unemployment remain higher (e.g,. MA expects Raleigh's unemployment rate to be about 6.2% for 2020 compared to 3.4% in 2019), it could make customers less able to absorb rate increases. Should this influence PSNC's next rate case outcome, the company's financial profile and cash flow ratios could remain weak for its current credit profile.

Governance

PSNC's governance is driven by that of Dominion Energy its ultimate parent company, a credit positive. Dominion's overall governance practices are strong, with alignment to credit supportive benchmarks regarding ownership, control, compliance and reporting practices. An area where disclosure could improve is in regard to strategic initiatives, such as public policies for Board approval of M&A transactions and asset sales or divestitures; especially since this is a focus of the company from time to time.

Liquidity analysis

PSNC depends upon its parent in order to maintain adequate liquidity. On a standalone basis, PSNC will continue to produce substantial free cash flow deficits, as its 2021 capex of nearly $300 million continues to outpace cash flow from operations, which we expect to be around $115 million for the year.

PSNC has a $400 million inter-company credit agreement, with outstanding amounts reflected as "accounts payable-affiliated companies" on PSNC's balance sheet. At 30 September 2020, PSNC had borrowings outstanding of around $123 million under this agreement. Dominion is also continually in a negative free cash flow position and relies on external credit and strong capital market support for its liquidity.

PSNC has $150 million of private placement bonds due in February of 2020, which we understand is being addressed currently and we expect to be refinanced. The next long-term debt maturity is $50 million due in January 2026.

Rating methodology and scorecard factors

Exhibit 5

Rating Factors

Public Service Co. of North Carolina, Inc.

Regulated Electric and Gas Utilities Industry [1][2]	Current LTM 9/30/2020		Moody's 12-18 Month Forward View As of Date Published [3]	
Factor 1 : Regulatory Framework (25%)	**Measure**	**Score**	**Measure**	**Score**
a) Legislative and Judicial Underpinnings of the Regulatory Framework	A	A	A	A
b) Consistency and Predictability of Regulation	Aa	Aa	Aa	Aa
Factor 2 : Ability to Recover Costs and Earn Returns (25%)				
a) Timeliness of Recovery of Operating and Capital Costs	A	A	A	A
b) Sufficiency of Rates and Returns	Baa	Baa	Baa	Baa
Factor 3 : Diversification (10%)				
a) Market Position	Ba	Ba	Ba	Ba
b) Generation and Fuel Diversity	N/A	N/A	N/A	N/A
Factor 4 : Financial Strength (40%)				
a) CFO pre-WC + Interest / Interest (3 Year Avg)	3.8x	Baa	3.5x - 4x	Baa
b) CFO pre-WC / Debt (3 Year Avg)	12.9%	Baa	10% - 13%	Baa
c) CFO pre-WC – Dividends / Debt (3 Year Avg)	10.4%	Baa	10% - 13%	Baa
d) Debt / Capitalization (3 Year Avg)	44.4%	A	40% - 45%	A
Rating:				
Scorecard-Indicated Outcome Before Notching Adjustment		Baa1		Baa1
HoldCo Structural Subordination Notching		0		0
a) Scorecard-Indicated Outcome		Baa1		Baa1
b) Actual Rating Assigned		Baa1		Baa1

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
[2] As of 9/30/2020(L)
[3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures.
[4] Low business risk for financial strength
Source: Moody's Financial Metrics

Appendix

Exhibit 6

Cash Flow and Credit Metrics

CF Metrics	Dec-16	Dec-17	Dec-18	Dec-19	LTM Sept-20
As Adjusted					
FFO	**152**	**171**	**128**	**127**	**148**
+/- Other	-24	-14	-15	-12	-33
CFO Pre-WC	**128**	**157**	**113**	**115**	**115**
+/- ΔWC	-15	-53	-21	11	-11
CFO	**113**	**103**	**92**	**126**	**104**
- Div	34	36	44	13	0
- Capex	171	276	244	168	219
FCF	**-92**	**-208**	**-196**	**-56**	**-115**
(CFO Pre-W/C) / Debt	22.2%	20.4%	12.1%	12.6%	11.8%
(CFO Pre-W/C - Dividends) / Debt	16.3%	15.7%	7.4%	11.2%	11.8%
FFO / Debt	26.4%	22.2%	13.7%	14.0%	15.3%
RCF / Debt	20.5%	17.5%	9.0%	12.6%	15.3%
Revenue	423	470	500	545	521
Interest Expense	26	33	42	44	43
Net Income	57	70	84	74	88
Total Assets	2,048	2,357	2,569	2,784	2,891
Total Liabilities	1,272	1,552	1,712	1,779	1,832
Total Equity	775	806	857	1,005	1,059

All figures and ratios are calculated using Moody's estimates and standard adjustments. Periods are Financial Year-End unless indicated. LTM = Last Twelve Months
Source: Moody's Financial Metrics

Exhibit 7

Peer Comparison Table

	Public Service Co. of North Carolina, Baa1 (Stable)			Piedmont Natural Gas Company, Inc. A3 (Stable)			DTE Gas Company A3 (Stable)			Spire Alabama Inc. A2 (Stable)		
(In US millions)	FYE Dec-18	FYE Dec-19	LTM Sept-20	FYE Dec-18	FYE Dec-19	LTM Sept-20	FYE Dec-18	FYE Dec-19	LTM Sept-20	FYE Sep-19	FYE Sep-19	LTM Pre20
Revenue	500	545	521	1,375	1,381	1,296	1,415	1,462	1,386	501	466	455
CFO Pre-W/C	113	115	115	285	475	418	337	368	427	137	176	174
Total Debt	934	911	970	2,395	2,906	3,146	1,826	1,997	2,102	521	624	678
CFO Pre-W/C + Interest / Interest	3.7x	3.6x	3.7x	3.9x	5.2x	4.0x	5.5x	5.5x	6.1x	7.9x	8.5x	8.2x
CFO Pre-W/C / Debt	12.1%	12.6%	11.8%	11.9%	16.3%	13.3%	18.5%	18.4%	20.3%	26.3%	28.3%	25.7%
CFO Pre-W/C – Dividends / Debt	7.4%	11.2%	11.8%	11.9%	16.3%	13.3%	12.3%	12.3%	14.0%	20.5%	25.2%	22.1%
Debt / Capitalization	47.2%	43.1%	43.4%	47.8%	48.3%	48.6%	43.9%	44.2%	44.0%	39.3%	43.0%	44.4%

All figures & ratios calculated using Moody's estimates & standard adjustments. FYE = Financial Year-End. LTM = Last Twelve Months.
Source: Moody's Financial Metrics

Ratings

Exhibit 8

Category	Moody's Rating
PUBLIC SERVICE CO. OF NORTH CAROLINA, INC.	
Outlook	Stable
Senior Unsecured	Baa1
ULT PARENT: DOMINION ENERGY, INC.	
Outlook	Stable
Senior Unsecured	Baa2
Jr Subordinate	Baa3
Pref. Stock	Ba1
Commercial Paper	P-2

Source: Moody's Investors Service

REPORT NUMBER 1260494

MOODY'S
INVESTORS SERVICE