

PLACE: Held via Videoconference

DATE: Friday, January 29, 2021

TIME: 9:00 a.m. - 12:30 p.m.

DOCKET NO. : E-2, Sub 1262

E-7, Sub 1243

BEFORE: Chair Charlotte A. Mitchell, Presiding

Commissioner Tola D. Brown-Bland

Commissioner Lyons Gray

Commissioner Daniel G. Clodfelter

Commissioner Kimberly W. Duffley

Commissioner Jeffrey A. Hughes

Commissioner Floyd B. McKissick, Jr.

IN THE MATTER OF:

Joint Petition of Duke Energy Carolinas, LLC,
and Duke Energy Progress, LLC, for Issuance of Storm
Recovery Financing Orders

VOLUME: 3



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1 P R O C E E D I N G S:

2 CHAIR MITCHELL: All right. Good
3 morning, everyone. Let's go on the record, please.
4 Before we begin this morning, I want to check in
5 with counsel to see if there are any preliminary
6 matters for my attention.

7 MR. ROBINSON: Nothing from the
8 Companies, Chair Mitchell.

9 CHAIR MITCHELL: Okay. Thank you,
10 Mr. Robinson.

11 Anything from the Public Staff,
12 Mr. Creech?

13 MR. CREECH: Not at this time.

14 CHAIR MITCHELL: Okay. All right.
15 Mr. Robinson, we are with you. You may call your
16 next witness.

17 MR. ROBINSON: Thank you,
18 Chair Mitchell. Quickly, before we call our next
19 witness, just to resolve yesterday's proceedings.
20 So it's our understanding that Mr. Atkins has
21 completed his testimony, unless the Commission had
22 any more questions for Mr. Atkins. So, at this
23 time, Chair Mitchell, Companies would move to
24 excuse Mr. Atkins. I believe, also, counsel did

1 move in his testimony and exhibits yesterday, but
2 just in the abundance of caution, if that did not
3 happen, I would move that as well.

4 CHAIR MITCHELL: All right.

5 Mr. Robinson, yes, and I should have been clearer
6 on the record yesterday. Mr. Atkins is excused,
7 and I will allow your motion to admit his testimony
8 and evidence into the record -- exhibits into the
9 record, having heard no objection from counsel.

10 MR. ROBINSON: Thank you,
11 Chair Mitchell. At this time, the Companies will
12 call Ms. Melissa Abernathy.

13 CHAIR MITCHELL: All right.

14 Ms. Abernathy, there are you.

15 Whereupon,

16 MELISSA ABERNATHY,

17 having first been duly affirmed, was examined
18 and testified as follows:

19 CHAIR MITCHELL: All right. Thank you.

20 You may proceed, Mr. Robinson.

21 DIRECT EXAMINATION BY MR. ROBINSON:

22 Q. Good morning, Ms. Abernathy. Please state
23 your full name and your business address for the
24 record.

1 A. My name is Melissa Abernathy, and my business
2 address is 550 South Tryon Street, Charlotte,
3 North Carolina.

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

6 A. I'm employed by Duke Energy Carolinas as
7 director of rates and regulatory planning for North and
8 South Carolina.

9 Q. Ms. Abernathy, did you cause to be prefiled
10 in this docket, 25 pages of direct testimony, and seven
11 exhibits for DEC, and seven exhibits for DEP?

12 A. I did.

13 Q. Do you have any changes or corrections to
14 your direct testimony or exhibits?

15 A. I do not.

16 Q. Are your -- are they true and correct to the
17 best of your knowledge?

18 A. They are.

19 Q. And if I asked you the same questions today,
20 would your answers be the same?

21 A. Yes, they would.

22 Q. Ms. Abernathy, did you also cause to be
23 prefiled rebuttal testimony consisting of 24 pages, and
24 five exhibits for DEC, and five exhibits for DEP?

1 A. Yes, I did.

2 Q. Do you have any changes or corrections to
3 your rebuttal testimony or exhibits?

4 A. No, I do not.

5 Q. Are they true and correct to the best of your
6 knowledge?

7 A. Yes, they are.

8 Q. And if I asked you the same questions today,
9 would your answers be the same?

10 A. Yes, they would.

11 MR. ROBINSON: Chair Mitchell, at this
12 time, I would ask that the prefilled direct and
13 rebuttal testimony and exhibits of Ms. Abernathy be
14 copied into the record as if given orally from the
15 stand today.

16 CHAIR MITCHELL: All right.

17 Mr. Robinson, hearing no objection to your motion,
18 the prefilled direct testimony of Melissa Abernathy
19 filed on October 26, 2020, in this docket,
20 consisting of 25 pages, shall be copied into the
21 record as if delivered orally from the stand. The
22 seven exhibits to that direct testimony shall be
23 marked as they were when they were prefilled.

24 Additionally, the 23 pages of rebuttal

1 testimony prefilled in this docket -- in these
2 dockets on January 11, 2021, shall be copied into
3 the record as if delivered orally from the stand,
4 and the five exhibits to that testimony shall be
5 marked as they were when they were prefilled.

6 (Abernathy DEC Exhibits 1 through 7,
7 Abernathy DEP Exhibits 1 through 7,
8 Abernathy DEC Rebuttal Exhibits 1
9 through 5, and Abernathy DEP Rebuttal
10 Exhibits 1 through 5, were identified as
11 they were marked when prefilled.)

12 (Whereupon, the prefilled direct and
13 rebuttal testimony of Melissa Abernathy
14 were copied into the record as if given
15 orally from the stand.)

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BEFORE THE NORTH CAROLINA UTILITIES COMMISSION**DOCKET NO. E-7, SUB 1243****DOCKET NO. E-2, SUB 1262**

In the Matter of:)	
	)	DIRECT TESTIMONY OF
Petition of Duke Energy Carolinas, LLC	)	MELISSA ABERNATHY
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

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. My name is Melissa Abernathy, and my business address is 550 South Tryon
3 Street, Charlotte, North Carolina.

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

5 A. I am a Director of Rates & Regulatory Planning for North Carolina and South
6 Carolina, employed by Duke Energy Carolinas, LLC (“DEC”), testifying on
7 behalf of DEC and Duke Energy Progress, LLC (“DEP”) (each a “Company”
8 or collectively “the Companies”).

9 **Q. PLEASE BRIEFLY SUMMARIZE YOUR EDUCATIONAL
10 BACKGROUND AND PROFESSIONAL EXPERIENCE.**

11 A. I graduated from the University of North Carolina at Chapel Hill with a
12 Bachelor of Science degree in Business Administration and Master of
13 Accountancy degree. I am a Certified Public Accountant licensed in the State
14 of North Carolina. My work experience prior to Duke Energy Corporation
15 (“Duke Energy”) was with Deloitte and Touche, LLP as an Audit Manager,
16 primarily serving clients in the energy industry. I began my employment with
17 Duke Energy in 2009 in the Corporate Audit Services Department and I joined
18 Asset Accounting in March 2015. In 2020, I moved to my current position in
19 the Rates Department as Director of Rates & Regulatory Planning and am
20 responsible for managing general rate cases, storm securitization and other
21 deferral reporting.

1 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE NORTH**
2 **CAROLINA UTILITIES COMMISSION (“COMMISSION”)?**

3 A. No.

4 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**
5 **PROCEEDING?**

6 A. The purpose of my testimony is to support the calculation of the DEC and DEP
7 revenue requirements for the proposed charges to customers necessary to pay
8 the storm recovery costs and financing costs of each Company, the “storm
9 recovery charges,” as a result of Hurricanes Florence, Michael, Dorian, and
10 Winter Storm Diego (“Storms”). The storm recovery costs consist of each
11 Company’s incremental operation and maintenance (“O&M”) expenses
12 deferred as regulatory assets as originally requested in each Storm Deferral
13 Docket (as defined below), as well as the associated capital investments
14 incurred during the Storms and accrued carrying charges.

15 The incremental O&M expenses and capital investments were the
16 subject of DEC’s Petition for An Accounting Order to Defer Incremental Storm
17 Damage Expenses Incurred filed in Docket No. E-7, Sub 1187 and DEP’s
18 Docket No. E-2, Sub 1193 (each, a “Storm Deferral Docket”). The Storm
19 Deferral Dockets for DEC and DEP were then consolidated into each
20 Company’s 2019 general rate cases in DEC Docket No. E-7, Sub 1214 and DEP
21 Docket No. E-2, Sub 1219 (“2019 Rate Cases”). In each Company’s
22 Agreement and Stipulation of Partial Settlement with the North Carolina

1 Utilities Commission—Public Staff (“Public Staff”) (each, a “Stipulation”),¹
 2 DEC and DEP agreed to remove capital investments and incremental O&M
 3 expenses and accrued carrying charges associated with the Storms from the
 4 2019 Rate Cases, and begin the process to seek recovery of the storm recovery
 5 costs in accordance with approved securitization financing orders under N.C.
 6 Gen. Stat. § 62-172 (the “Securitization Statute”). In addition, the Public Staff,
 7 through the 2019 Rate Cases, reviewed the costs of the Storms and filed
 8 testimony stating that the costs were prudently incurred.² At this time, the
 9 Company is still awaiting an order in the 2019 Rate Cases with the
 10 determination that the storm costs were reasonable and prudent and will not
 11 proceed with securitizing until such an order is received and the Commission
 12 approves DEC and DEP’s proposed Financing Orders provided as exhibits to
 13 the Companies’ Joint Petition for Financing Orders (“Joint Petition”).

14 The proposed storm recovery charges are independent of and
 15 incremental to DEC and DEP’s North Carolina retail base rates. The proposed
 16 storm recovery charges are usage-based charges that under the Securitization
 17 Statute, would be required to be paid by all existing or future retail customers
 18 receiving transmission or distribution service, or both, from DEC or DEP or its
 19 successors or assignees under Commission-approved rate schedules or under

¹ The Stipulations for DEC and DEP were filed on March 25, 2020 and June 2, 2020, respectively.

² See Direct Testimony of Michelle M Boswell on Behalf of the Public Staff, at 27-28, Docket No. E-7, Sub 1214 (filed Feb. 18, 2020); Direct Testimony of Shawn L. Dorgan on Behalf of the Public Staff, at 32, Docket No. E-2, Sub 1219 (filed Apr. 13, 2020); Supplemental Direct Testimony of Shawn L. Dorgan on Behalf of the Public Staff, at 9, Docket No. E-2, Sub 1219 (filed Apr. 23, 2020).

1 special contracts. The testimony of witness Jonathan Byrd discusses the
2 calculation of the storm recovery charges by rate class.

3 As discussed in witness Thomas J. Heath, Jr.'s testimony, each
4 Company is proposing the use of the proceeds from the sale of a series of storm
5 recovery bonds as the recommended method of recovering storm related
6 deferred expenses, capital investments, accrued carrying charges and financing
7 costs after considering the traditional method of recovering such costs. Based
8 on current market conditions, I will demonstrate that the issuance of storm
9 recovery bonds and the imposition of the relevant storm recovery charges are
10 expected to provide quantifiable benefits to customers of each Company as
11 compared with the traditional method of financing and recovering storm
12 recovery costs (the "Traditional Recovery Method" which is discussed later in
13 my testimony).

14 **Q. WHAT IS THE SCOPE OF YOUR TESTIMONY?**

15 A. My testimony is principally devoted to: (i) identifying and estimating the
16 revenue requirement necessary to recover the storm recovery costs that each
17 Company proposes to finance using storm recovery bonds and recover through
18 storm recovery charges; (ii) providing a comparison between the net present
19 value of the costs to customers that are estimated to result from the issuances
20 of storm recovery bonds and the costs that would result from the application of
21 the Traditional Recovery Method; (iii) describing changes in storm recovery
22 costs since the last update in the 2019 Rate Cases; (iv) describing the allocation

1 methodology for the storm recovery charges; and (v) addressing whether the
2 Companies plan to establish a storm recovery reserve at this time.

3 Barring significant changes in the terms of an issuance of storm
4 recovery bonds, or significant changes in embedded benchmark interest rates
5 or credit spreads of securitization bonds, the results presented in my testimony,
6 including the revenue requirement for the proposed storm recovery charges,
7 should closely approximate the final figures.

8 My testimony addresses the following subject areas:

- 9 • A description of DEC and DEP's storm recovery costs proposed for storm
10 recovery cost financings;
- 11 • Discussion of changes in estimates of the storm recovery costs since the
12 last update in the Companies' 2019 Rate Cases;
- 13 • A description of the allocation methodology used for the storm recovery
14 charges;
- 15 • A calculation demonstrating quantifiable benefits to customers in
16 accordance with N.C. Gen. Stat. § 62-172(b)(1)g. The Companies will
17 show scenarios consistent with the terms agreed to in the Stipulations that
18 the net present value of the costs to customers under the proposed issuance
19 of storm recovery bonds and imposition of storm recovery charges is less
20 than the net present value of the costs that would result under traditional
21 storm cost recovery; and
- 22 • Discussion regarding the application of a storm recovery reserve.

1 **Q. ARE YOU SPONSORING ANY EXHIBITS TO YOUR DIRECT**
2 **TESTIMONY?**

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

- 5 • Abernathy Exhibit 1 – Schedule of NC Retail Total Revenue Requirement
6 for Storm Recovery Charges
- 7 • Abernathy Exhibit 2 – Reconciliation of Rate Case Storm Recovery Costs
8 to Projected Storm Recovery Costs to be Securitized
- 9 • Abernathy Exhibit 3 – Allocation of Storm Recovery Charge to Customer
10 Classes
- 11 • Abernathy Exhibit 4 – Actual Storm Cost Recovery Charges Annual
12 Revenue Requirement - Storm Recovery Charge Model
- 13 • Abernathy Exhibit 5 – Traditional Recovery Model versus Storm Recovery
14 Charge Model - Quantifiable Benefit to Customers
- 15 • Abernathy Exhibit 6 – Annual Revenue Requirement - Traditional
16 Recovery Model, with supporting schedules
- 17 • Abernathy Exhibit 7 – Annual Revenue Requirement - Traditional
18 Recovery Model, with supporting schedules

19 Each of these exhibits were prepared under my direction and control, and
20 to the best of my knowledge all factual matters contained therein are true and
21 accurate.

1 **II. STORM RECOVERY COSTS**

2 **Q. WHAT IS THE DEFINITION OF STORM RECOVERY COSTS?**

3 A. As defined under the Securitization Statute:

4 “Storm recovery costs means all of the following:

- 5 a. All incremental costs, including capital investments, appropriate for
6 recovery from existing and future retail customers receiving
7 transmission or distribution service from the public utility that a
8 public utility has incurred or expects to incur as a result of the
9 applicable storm that are caused by, associated with, or remain as a
10 result of undertaking storm recovery activity. Such costs include the
11 public utility's cost of capital from the date of the applicable storm
12 to the date the storm recovery bonds are issued calculated using the
13 public utility's weighted average cost of capital as defined in its most
14 recent base rate case proceeding before the Commission net of
15 applicable income tax savings related to the interest component.
- 16 b. Storm recovery costs shall be net of applicable insurance proceeds,
17 tax benefits and any other amounts intended to reimburse the public
18 utility for storm recovery activities such as government grants, or
19 aid of any kind and where determined appropriate by the
20 Commission, and may include adjustments for capital replacement
21 and operating costs previously considered in determining normal
22 amounts in the public utility's most recent general rate proceeding.
23 Storm recovery costs includes the cost to replenish and fund any
24 storm reserves and costs of repurchasing equity or retiring any
25 existing indebtedness relating to storm recovery activities.
- 26 c. With respect to storm recovery costs that the public utility expects
27 to incur, any difference between costs expected to be incurred and
28 actual, reasonable and prudent costs incurred, or any other rate-
29 making adjustments appropriate to fairly and reasonably assign or
30 allocate storm cost recovery to customers over time, shall be
31 addressed in a future general rate proceeding, as may be facilitated
32 by other orders of the Commission issued at the time or prior to such
33 proceeding; provided, however, that the Commission's adoption of
34 a financing order and approval of the issuance of storm recovery
35 bonds may not be revoked or otherwise modified.”

1 **Q. DO THE COST AMOUNTS CONTAINED IN DEC AND DEP'S STORM**
2 **RECOVERY COSTS, AS DEFINED IN DIRECT TESTIMONY FILED**
3 **IN EACH COMPANY'S 2019 RATE CASES, MEET THE DEFINITION**
4 **OF STORM RECOVERY COSTS PURSUANT TO THE**
5 **SECURITIZATION STATUTE?**

6 A. Yes, for several reasons. First, the costs incurred by each Company that
7 comprise the storm recovery costs are related to the incremental O&M expense
8 and capital investments associated with the Storms. These costs include each
9 Company's cost of capital, from the date of the storms to the date the storm
10 recovery bonds are issued, using weighted average cost of capital ("WACC")
11 as defined in the most recent base rate case, net of applicable income tax savings
12 related to the interest component. Also, all storm recovery costs are net of
13 applicable insurance proceeds. Finally, the costs eligible for recovery pursuant
14 to the Securitization Statute that are included in the storm recovery costs are
15 reduced by the highest amount within the normal range of fluctuation included
16 in each Company's 2019 Rate Case at the time of the Storms.

17 **Q. PLEASE DESCRIBE THE COSTS THAT MAKE UP THE DEC AND**
18 **DEP STORM RECOVERY COSTS TO BE SECURITIZED.**

19 A. The DEC and DEP storm recovery costs to be securitized are made up of the
20 components presented for each Company in their respective 2019 Rate Case
21 dockets. As I mentioned previously, the Public Staff found the storm recovery
22 costs to be prudently incurred in each Company's 2019 Rate Case.

1 Consequently, in each Company's Stipulation, the parties agreed to remove
2 deferred incremental O&M expenses, accrued carrying charges and storm
3 capital investments from DEC and DEP's respective rate cases. The following
4 balances were removed from the rate cases per each Company's Stipulation: a
5 projected balance as of July 31, 2020 for DEC of approximately \$213 million
6 and a projected balance as of August 31, 2020 for DEP of approximately \$714
7 million. Abernathy Exhibit 2 attached to my direct testimony in this filing
8 provides the breakdown of these amounts between incremental O&M expenses,
9 capital investments, and accrued carrying charges. Abernathy Exhibit 2 also
10 provides a reconciliation of storm recovery costs as of the date of the last update
11 in each Company's 2019 Rate Case to the storm recovery costs projected
12 through May 31, 2021 to be recovered using storm recovery bonds. This
13 includes a reduction to the estimates included in the 2019 Rate Cases, which is
14 discussed later in my testimony. The storm recovery costs to be securitized also
15 include carrying charges to the date of the bond issuance, which is expected to
16 be June 1, 2021. The total projected storm recovery costs to be financed using
17 storm recovery bonds through May 31, 2021 are included in Abernathy Exhibit
18 2 attached to my direct testimony in this filing. Abernathy Exhibit 1 attached
19 to my direct testimony includes the upfront financing costs that will also be
20 financed using storm recovery bonds.

1 **Q. WERE ANY OF THE STORM RECOVERY COSTS THAT WERE**
2 **INCLUDED IN THE 2019 RATE CASES CONSIDERED TO BE**
3 **ESTIMATES WITH STORM RECOVERY ACTIVITIES STILL BEING**
4 **UNDERTAKEN, BUT NOT COMPLETED?**

5 A. Yes. The storm recovery cost estimates have continued to be refined after the
6 Stipulation was reached in each Company's 2019 Rate Case, primarily for
7 DEP's 2019 Hurricane Dorian. In addition, there were small adjustments
8 related to the 2018 Storms as the cost estimates and remaining invoices were
9 finalized and the 2018 storm projects were closed. These adjustments are
10 included in the amounts included in this Joint Petition. Accordingly, the
11 incremental O&M estimate for DEP decreased approximately \$11 million since
12 the last update in DEP's 2019 Rate Case. The incremental O&M estimate for
13 DEC has decreased by approximately \$31 thousand. Each Company's storm
14 recovery costs to be recovered through the storm recovery bonds has been
15 adjusted since the Stipulations were filed to reflect the refinement of these
16 estimates, which is reflected in Exhibit 2, attached to my direct testimony, for
17 DEC and DEP. No further adjustments to incremental O&M or capital costs
18 included in this securitization financing are expected.

1 **Q. PLEASE INDICATE WHETHER EACH COMPANY PROPOSES TO**
2 **FINANCE ALL OR A PORTION OF ITS STORM RECOVERY COSTS**
3 **INCLUDED IN THE 2019 RATE CASE REQUESTS USING STORM**
4 **RECOVERY BONDS.**

5 A. DEC and DEP propose to finance the entire balance of their respective storm
6 recovery costs. It should be noted that the storm recovery cost balances as of
7 the Joint Petition date, October 26, 2020, include increases for estimated
8 carrying charges through May 31, 2021 (the expected issuance date of the storm
9 recovery bonds).

10 **Q. PLEASE DESCRIBE OTHER COSTS THAT ARE INCLUDED IN THE**
11 **SECURITIZABLE BALANCE OF THE STORM RECOVERY BONDS**
12 **AND THE REVENUE REQUIREMENT FOR THE STORM**
13 **RECOVERY CHARGES.**

14 A. Up-Front financing costs are added to the projected storm recovery costs to
15 arrive at the total Securitizable Balance for the storm recovery bonds. These
16 amounts are quantified and described by witness Heath and are included in
17 Abernathy Exhibit 1 to arrive at the total Securitizable Balance for the storm
18 recovery bonds of approximately \$230.8 million for DEC and \$748.0 million
19 for DEP. Estimates of on-going financing costs are also included in the revenue
20 requirement for the storm recovery charges. These amounts are also quantified
21 and described by witness Heath and are included in Abernathy Exhibit 1.
22 Including the estimates of on-going financing costs, Abernathy Exhibit 1

1 calculates the total revenue requirement related to storm securitization to be
2 approximately \$262.1 million for DEC and \$842.0 million for DEP. Abernathy
3 Exhibit 4 shows this revenue requirement by year for the 15-year amortization
4 period.

5 **Q. PLEASE DESCRIBE EACH COMPANY'S REQUIREMENTS UNDER**
6 **THE STIPULATIONS TO FINANCE THE STORM RECOVERY**
7 **COSTS.**

8 A. DEC and DEP are required to demonstrate quantifiable benefits to its customers
9 in accordance with N.C. Gen. Stat. § 62-172(b)(1)g. Specifically, each
10 Company must show that the net present value of the costs to its customers from
11 an issuance of storm recovery bonds is less than the net present value of the
12 costs that would result under the Traditional Recovery Method. To achieve
13 this, for the storm recovery costs related to these Storms only, each Company
14 agreed in their respective Stipulations that when conducting this comparison,
15 the following assumptions with respect to new rates that would be imposed in
16 connection with the Traditional Recovery Method and in the absence of the
17 issuance of storm recovery bonds shall be made:

- 18 • For the Traditional Recovery Method, 12 months of amortization for each
19 Storm was expensed prior to the new rates going into effect;
- 20 • For the Traditional Recovery Method, no capital costs incurred due to the
21 Storms during the 12-month period were included in the deferred balance;
- 22 • For the Traditional Recovery Method, no carrying charges were accrued

1 on the deferred balance during the 12-month period following the date(s)
2 of the Storm(s);

- 3 • For the Traditional Recovery Method, the amortization period for the
4 Storms is a minimum of 10 years for DEC and 15 years for DEP; and
- 5 • For securitization, the imposition of the storm recovery charge begins nine
6 months after the new rates go into effect

7 **Q. WHAT AMORTIZATION PERIOD IS EACH COMPANY PROPOSING**
8 **UNDER THE STORM RECOVERY MODEL?**

9 A. Each Company is proposing a 15-year amortization period under the Storm
10 Recovery Model.

11 **Q. HOW DO THE COMPANIES PROPOSE TO TREAT CARRYING**
12 **CHARGES ON THE STORM RECOVERY COSTS?**

13 A. Given that each Company will incur carrying charges until the date of the bond
14 issuance, each Company will reflect the actual carrying charges at the time of
15 its bond issuance in its bond issuance amount. The carrying charges include
16 each Company's cost of capital from the date of the applicable storm to the date
17 the storm recovery bonds are issued, calculated using each Company's most
18 recently approved WACC, net of applicable income tax savings related to the
19 interest component. The WACC rates for DEC and DEP last approved by the
20 Commission in Docket Nos. E-7, Sub 1146 and E-2, Sub 1142 are 6.84 percent
21 and 6.64 percent, respectively. These rates will be used until the Commission
22 issues orders in the 2019 Rate Cases approving new WACCs. At that time,

1 each Company will update the WACC rates to those approved. The updated
2 WACC rates will be used to calculate projected carrying charges on the balance
3 of the storm recovery costs as of the expected new rates effective date for each
4 Company. For purposes of calculating total expected carrying costs, DEC has
5 assumed an expected new rates effective date of January 1, 2021 and DEP has
6 assumed an expected new rates effective date of February 1, 2021. If the
7 expected new rates effective dates change, the carrying charges will be updated
8 for each Company after the Commission's Order. Additionally, when
9 estimating total expected carrying charges, DEC and DEP used WACC rates of
10 6.56 percent and 6.48 percent, respectively, based on the Second Partial
11 Stipulation Agreements with the Public Staff filed as part of the 2019 Rate
12 Cases starting at the assumed new rates effective dates stated above. The
13 carrying charges will be updated for each Company if the approved WACC
14 rates differ from these assumptions.

15 **Q. HAVE THE COMPANIES INCLUDED ESTIMATED CARRYING**
16 **CHARGES BEYOND MAY 2021 FOR PURPOSES OF CALCULATING**
17 **REVENUE REQUIREMENTS AND CUSTOMER RATE IMPACTS IN**
18 **THIS FILING?**

19 A. No. All of the calculations of revenue requirements and rate impacts under the
20 proposed imposition of storm recovery charges do not include any carrying
21 charges beyond May 31, 2021. As further explained in witness Heath's
22 testimony, the Company will work to issue the storm recovery bonds as soon

1 as practicable and prior to May 31, 2021. Since the issuance date is not certain,
2 carrying charges beyond May 31, 2021 have not been estimated. However, the
3 storm recovery costs will continue to increase until the financing is complete.
4 Any delays in the debt issuance past May 31, 2021 will result in higher accrued
5 carrying charges and an ultimately higher bond issuance amount than the
6 amounts that have been included in the Joint Petition and relevant exhibits. For
7 DEC, the balance will increase by approximately \$1 million per month from the
8 projected \$226 million balance of storm recovery costs as of May 31, 2021. For
9 DEP, the balance will increase by approximately \$4 million per month from the
10 projected \$739 million balance of storm recovery costs as of May 31, 2021.

11 **Q. PLEASE DESCRIBE THE TRUE-UP MECHANISM FOR THE**
12 **ESTIMATES OF UP-FRONT AND ON-GOING FINANCING FEES, AS**
13 **OF THE DATE OF THE JOINT PETITION, THAT WILL IMPACT**
14 **THE REVENUE REQUIREMENT FOR THE COMPANIES, AND**
15 **SPECIFICALLY HOW TRUE-UPS TO THE ESTIMATES ARE**
16 **RECOVERED BY THE COMPANIES OR RETURNED TO**
17 **CUSTOMERS.**

18 A. The proceeds of the storm recovery bond issuance will be used to pay (or
19 reimburse) the Companies for the actual up-front financing costs incurred. Up-
20 front and on-going financing costs are discussed in more detail in witness
21 Heath's direct testimony. Since actual up-front financing costs will not be
22 known until after the Commission issues the Financing Orders and the storm

1 recovery bonds have been issued, if the actual up-front financing costs are
2 below the amount appearing in the issuance advice letter filed with the
3 Commission, then the difference will be credited back to customers in the true-
4 up adjustment letter as discussed in the proposed Financing Orders.
5 Conversely, if the actual up-front financing costs are in excess of the amounts
6 appearing in the issuance advice letter, the Companies have no ability to collect
7 this excess amount through the storm recovery charge. Therefore, in the Joint
8 Petition, the Companies are seeking permission to establish a regulatory asset
9 to defer any prudently incurred excess amounts of up-front financing costs to
10 preserve for later recovery in their next respective general rate case proceeding.

11 Witness Shana Angers discusses in her direct testimony the true-up
12 mechanism to ensure the recovery of revenues associated with the on-going
13 financing costs payable in connection with the storm recovery bonds.

14 **III. STORM RECOVERY RESERVE**

15 **Q. AS ALLOWED BY THE SECURITIZATION STATUTE, DO THE**
16 **COMPANIES PROPOSE TO ESTABLISH OR FUND A LEVEL OF**
17 **STORM RECOVERY RESERVE TO BE RECOVERED THROUGH**
18 **THE STORM RECOVERY BONDS?**

19 **A.** No, not at this time.

1 **IV. ALLOCATION METHODOLOGY OF THE STORM**

2 **RECOVERY CHARGE**

3 **Q. HOW DO DEC AND DEP PROPOSE TO ALLOCATE THE COSTS**
4 **RECOVERABLE BY THE PROPOSED ISSUANCE OF STORM**
5 **RECOVERY BONDS AND IMPOSITION OF THE STORM**
6 **RECOVERY CHARGES TO THE RATE CLASSES?**

7 A. Each Company proposes to allocate the costs recoverable through the issuance
8 of storm recovery bonds in the same manner the costs were allocated in DEC
9 and DEP's most recent pending 2019 Rate Cases before the costs were
10 removed. Specifically, the distribution-related costs are allocated based on a
11 composite distribution plant allocator and the transmission-related costs are
12 allocated based on a transmission demand factor, both from the 2019 Rate
13 Cases. Abernathy Exhibit 3, which is attached to my direct testimony in this
14 filing, provides details of how the storm recovery charge will be allocated to
15 each of the customer classes.

1 **V. COMPARISON OF THE STORM RECOVERY CHARGE**
2 **MODEL TO THE TRADITIONAL RECOVERY METHOD AND**
3 **QUANTIFIABLE BENEFITS TO CUSTOMERS**

- 4 **Q. PLEASE DESCRIBE HOW STORM CHARGES TYPICALLY PASS TO**
5 **CUSTOMERS THROUGH A TRADITIONAL RECOVERY MODEL.**
- 6 A. While the Public Staff and the Company disagree³ on how storm costs should
7 be treated under the Traditional Recovery Model during a deferral period, prior
8 to the first rate case following a storm, the two parties do not disagree on the
9 treatment in or after that first rate case. Typically, in a Traditional Recovery
10 Model, a utility would request permission to defer storm costs to a regulatory
11 asset on the balance sheet to be amortized over an approved multi-year
12 amortization period. Both the unamortized regulatory asset and the
13 undepreciated capital assets are included in rate base. Accordingly, customers
14 pay a return on these balances at the utility's WACC. The WACC is comprised
15 of the utility's return on equity, embedded debt cost and capital structure
16 approved in the utility's most recent general rate case. In a Traditional
17 Recovery Model, the utility would receive from its customers a monthly
18 payment over the life of the regulatory asset and over the life of the capital
19 assets, which includes a revenue requirement for the amortization expense of
20 the regulatory asset, depreciation expense for the capital assets, and the return
21 component as described above.

1 **Q. DESCRIBE HOW STORM CHARGES PASS TO CUSTOMERS**
2 **THROUGH A STORM RECOVERY CHARGE MODEL?**

3 A. As explained more fully in witness Charles N. Atkins II's testimony, in a storm
4 recovery charge model, or financing of storm costs, the utility seeks to
5 accelerate the recovery of storm costs by issuing storm recovery bonds and
6 receiving one lump sum of cash upon issuance. The benefit to customers is that
7 the carrying charges are reduced to the sum of the carrying charges through the
8 date of the issuance of storm recovery bonds and not over the life or
9 amortization period of the associated assets. The revenue requirement for the
10 customer in a storm recovery charge model is for the debt service payments,
11 which would include principal, interest and various financing costs. Typically,
12 the interest expense on the AAA-rated securitization bonds in a storm recovery
13 charge model results in a much lower rate to customers than in the Traditional
14 Recovery Model that includes a WACC return over the life of the regulatory
15 and capital assets. Customer benefits or savings are driven by the difference
16 between the Company's WACC and the interest rate on AAA-rated
17 securitization bonds.

³ These differences are documented in parties' comments from DEP's 2016 rate case, Docket No. E-2, Sub 1142, as well as each Company's 2018 storm deferral petitions, Docket No. E-7, Sub 1187 and Docket No. E-2, Sub 1193.

1 **Q. PLEASE DESCRIBE HOW THE STIPULATIONS WITH THE PUBLIC**
2 **STAFF FOR EACH COMPANY IMPACTS THE CALCULATION OF**
3 **THE REVENUE REQUIREMENT UNDER THE TRADITIONAL**
4 **RECOVERY MODEL.**

5 A. As I mentioned earlier, the Public Staff and the Companies have different
6 perspectives on how the storm costs should be treated prior to the first rate case
7 following the Storms. In the Stipulations, to resolve these differences, for the
8 purpose of showing a comparison to traditional cost recovery in this
9 securitization petition, the parties agreed in the Traditional Recovery Model to
10 expense and not defer 12-months of amortization expense prior to the first rate
11 case, and agreed to expense and not defer 12-months of capital costs prior to
12 the first rate case. The parties also agreed that the 12-months of expenses would
13 not be reflected in the revenue requirement under the Traditional Recovery
14 Model. The parties also agreed to show the rate case rates effective date 12
15 months after the date of the 2018 storms and show the date of the securitization
16 9 months after that. Abernathy Exhibit 6 attached to my direct testimony shows
17 the calculation of the revenue requirement for the Traditional Recovery Model
18 consistent with the terms of the Stipulations.

19 **Q. PLEASE DESCRIBE THE KEY DATES AND ASSUMPTIONS IN THE**
20 **TRADITIONAL RECOVERY MODEL CALCULATION.**

21 A. First, for purposes of adhering to the Stipulations, the dates of the Storms were
22 assumed to be December 31, 2018, with a new rates effective date in the

1 ongoing 2019 Rate Cases of January 1, 2020 and an issuance of storm recovery
2 bonds on October 1, 2020. Additionally, each Company assumed a projected
3 pre-tax WACC and composite tax rate from its 2019 Rate Case proceeding
4 consistent with the Second Stipulations of Partial Settlement with the Public
5 Staff. For incremental O&M storm costs, the amortization period is assumed
6 to be 15 years for each Company, which is the same amortization period that is
7 to be used for the issuance of storm recovery bonds. For storm capital
8 investments, the depreciation rate was assumed to be 2.5 percent over a 40-year
9 life.

10 **Q. IF ACTUAL DATES HAD BEEN USED, WOULD EACH COMPANY**
11 **HAVE MORE OR LESS ANNUAL REVENUE REQUIREMENT AS A**
12 **RESULT AND DO THESE ASSUMPTIONS IMPACT SAVINGS TO**
13 **CUSTOMERS?**

14 A. Temporary rates in the pending 2019 Rate Cases were effective August 24,
15 2020 for DEC and September 1, 2020 for DEP. The actual expected date for
16 the securitization financing is June 1, 2021, approximately nine months after
17 the 2019 Rate Case temporary rates effective date. In addition, for DEP, one of
18 the storms, Hurricane Dorian, occurred in late 2019, not late 2018. If these
19 actual dates were used in the comparative analysis and, consistent with the
20 Stipulations, up to 12-months of amortization expense and capital costs were
21 excluded from the revenue requirements if occurring before the first rate case,
22 the revenue requirement for both models would have increased, primarily due

1 to more accrued carrying charges, but the comparison of the two models would
2 still show savings to customers by using the storm recovery charge model as
3 compared to the Traditional Recovery Model.

4 **Q. PLEASE DESCRIBE HOW ACCUMULATED DEFERRED INCOME**
5 **TAXES (“ADIT”) ARE A COMPONENT OF THE CALCULATION OF**
6 **QUANTIFIABLE BENEFITS TO CUSTOMERS IN THE**
7 **TRADITIONAL RECOVERY MODEL AND THE STORM RECOVERY**
8 **CHARGE MODEL.**

9 A. ADIT are deferred tax assets or liabilities resulting from timing differences
10 between the method of computing taxable income for reporting to the Internal
11 Revenue Service and the method of computing taxable income for accounting
12 purposes. The deferred expenses in the regulatory asset for storms creates an
13 ADIT liability. As shown in Abernathy Exhibits 6 and 7, under both the
14 Traditional Recovery Model and the storm recovery charge model, this ADIT
15 liability is a reduction to rate base, reducing the amount of return included in a
16 revenue requirement. In the storm recovery charge model, once storm recovery
17 bonds are issued and cash is received by each Company, the regulatory asset is
18 removed from each Company’s balance sheet. However, the ADIT credit
19 associated with the regulatory asset remains on the Company’s books and
20 continues to be a reduction to rate base for the customer.

1 **Q. USING THE ASSUMPTIONS AGREED TO IN THE STIPULATIONS,**
2 **WHAT IS THE TOTAL ESTIMATED NET PRESENT VALUE OF THE**
3 **COSTS TO CUSTOMERS THAT RESULT FROM THE ISSUANCE OF**
4 **STORM RECOVERY BONDS AND THOSE THAT RESULT FROM**
5 **THE APPLICATION OF THE TRADITIONAL RECOVERY**
6 **METHOD?**

7 A. The total estimated net present value (“NPV”) of the costs to customers is
8 provided in Abernathy Exhibit 5. For DEC, by using the storm recovery charge
9 model, the estimated NPV is approximately \$122 million based on market
10 conditions that existed as of the date of the Joint Petition. By contrast, under
11 the Traditional Recovery Method, the estimated NPV is approximately \$180
12 million. The difference is approximately \$58 million, or 32%. For DEP, under
13 the storm recovery charge model, the estimated NPV is \$400 million based on
14 market conditions that existed as of the date of the Joint Petition. By contrast,
15 the estimated NPV under the Traditional Recovery Method, is \$599 million.
16 The difference is approximately \$199 million, or 33%.

17 **Q. HOW WILL STORM COSTS BE RECOVERED IF THE COMMISSION**
18 **DOES NOT APPROVE FINANCING ORDERS FOR THE ISSUANCE**
19 **OF STORM RECOVERY BONDS OR IF DEC AND DEP ARE NOT**
20 **ABLE TO ISSUE THE STORM RECOVERY BONDS?**

21 A. As stated in each Company’s Stipulation with the Public Staff, a storm recovery
22 rider initially set at \$0 will be established as a result of the 2019 Rate Cases. In

1 the event that the Commission would ultimately reject DEC and DEP's Joint
2 Petition for the issuance of storm recovery bonds, or should the Companies be
3 otherwise unable to recover the costs of the Storms through the Securitization
4 Statute, the Company may request recovery of the costs of the Storms from the
5 Commission by filing a petition requesting an adjustment to this storm recovery
6 rider. In such case, both the Public Staff and each Company reserve the right
7 to argue their respective positions regarding the appropriate ratemaking
8 treatment for recovering the costs of the Storms.

9 **VI. CONCLUSION**

10 **Q. PLEASE SUMMARIZE YOUR TESTIMONY.**

11 A. I have provided support for the storm recovery costs that DEC and DEP each
12 propose to finance using storm recovery bonds, and for the methodology used
13 to allocate these costs by rate class. I have also discussed how the total NPV of
14 the costs to customers that are estimated to result from the issuance of storm
15 recovery bonds compares with the costs that would result from the application
16 of the Traditional Recovery Method under the agreed upon Stipulation
17 assumptions. Last, I have discussed how the imposition of storm recovery
18 charges are expected to provide quantifiable benefits to customers as compared
19 to costs that would be incurred absent the issuance of storm recovery bonds.

20 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

21 A. Yes.

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	)	MELISSA ABERNATHY
And Duke Energy Progress, LLC for	)	FOR DUKE ENERGY
Issuance of Storm Cost Recovery Financing	)	CAROLINAS, LLC AND DUKE
Orders	)	ENERGY PROGRESS, LLC

1 **I. INTRODUCTION**

2 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

3 A. My name is Melissa Abernathy, and my business address is 550 South Tryon
4 Street, Charlotte, North Carolina.

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

6 A. I am a Director of Rates & Regulatory Planning for North Carolina and South
7 Carolina, employed by Duke Energy Carolinas, LLC (“DEC”), testifying on
8 behalf of DEC and Duke Energy Progress, LLC (“DEP”) (each a “Company”
9 or collectively “the Companies”).

10 **Q. DID YOU PREVIOUSLY FILE TESTIMONY IN THIS PROCEEDING?**

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

12 **Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?**

13 A. The purpose of my rebuttal testimony is to: (1) respond to certain accounting
14 recommendations proposed by the Public Staff in its direct testimony; (2)
15 respond to Saber Partners, LLC’s (“Public Staff Consultants”) comments
16 related to the quantifiable customer benefit calculations provided in Abernathy
17 Exhibits 5-7 for both DEC and DEP; (3) provide exhibits showing the
18 calculation of quantifiable benefits to customers assuming a 20-year bond
19 period; and (4) respond to the Public Staff’s request to audit updated storm
20 costs.

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

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

- 5 • Abernathy Rebuttal Exhibit 1 – Updated Traditional Recovery Model
6 versus Storm Recovery Charge Model - Quantifiable Benefit to Customers
7 – 15-year bond term
- 8 • Abernathy Rebuttal Exhibit 2 – Updated Annual Revenue Requirement -
9 Traditional Recovery Model, with supporting schedules
- 10 • Abernathy Rebuttal Exhibit 3 – Updated Annual Revenue Requirement -
11 Storm Recovery Charge Model – 15-year bond term
- 12 • Abernathy Rebuttal Exhibit 4 – Traditional Recovery Model versus Storm
13 Recovery Charge Model – Quantifiable Benefit to Customers – 20-year
14 bond term
- 15 • Abernathy Rebuttal Exhibit 5 – Annual Revenue Requirement – Storm
16 Recovery Charge Model – 20-year bond term

17 Each of these exhibits were prepared under my direction and control, and to the
18 best of my knowledge all factual matters contained therein are true and accurate.

1 **II. PUBLIC STAFF ACCOUNTING RECOMMENDATIONS**

2 **Q. PLEASE PROVIDE AN OVERVIEW OF THE PUBLIC STAFF’S**
3 **ACCOUNTING RECOMMENDATIONS.**

4 A. The Public Staff makes several accounting recommendations regarding the
5 potential over- or under-recoveries of the Companies’ up-front and on-going
6 financing costs, potential over-collections of tail-end collections, and over-
7 recoveries of the servicing and administration fees. Specifically, regarding up-
8 front financing costs, the Public Staff recommends that for under-recoveries,
9 the regulatory asset that the Companies proposed to establish include only the
10 excess costs, adjusted if appropriate for income taxes, and accrued carrying
11 costs at the Companies’ respective net-of-tax weighted average cost of capital
12 (“WACC”), and collected in each of the Companies’ next general rate cases.
13 For over-recoveries of up-front financing costs, the Public Staff recommends
14 that these amounts be credited back to customers through use of a deferred
15 regulatory liability and subsequent credit to the Companies’ cost of service, in
16 each of the Companies’ next general rate cases.

17 For tail-end collections, the Public Staff recommends that any
18 overcollection be held in a regulatory liability account, separate from other
19 securitization-related regulatory assets and liabilities, and adjusted if
20 appropriate for income taxes and accrued carrying costs at the Companies’
21 respective net-of-tax WACC, and then refunded to customers in the
22 Companies’ next general rate cases. For on-going financing costs, the Public

1 Staff argues that adjustments that are passed through to the non-bypassable
2 storm recovery charges be matched with an offsetting regulatory asset or
3 liability in the Companies' traditional ratemaking cost of service. Last,
4 regarding servicing and administration fees, the Public Staff argues that these
5 costs should be held in a regulatory liability account, separate from the
6 regulatory assets and liabilities of other types of securitization-related costs and
7 benefits, adjusted if appropriate for income taxes and accrued carrying costs at
8 the Companies' respective net-of-tax WACC, and refunded to customers in the
9 Companies' next respective general rate cases.

10 For the reasons I explain below, the Companies agree with the Public
11 Staff's recommendations related to the under-recovery of up-front financing
12 costs and tail-end collections. However, the Companies do not agree with the
13 Public Staff's recommendation to establish a regulatory liability for the over-
14 recovery of up-front financing costs and the recommendations related to on-
15 going financing costs. In addition to my reasons, Companies witness Thomas
16 J. Heath, Jr. further explains why the Public Staff's recommendations regarding
17 up-front financing costs and on-going financing costs should be denied from
18 his perspective. Last, the Companies do not believe the Public Staff's
19 recommendations related to servicing and administration fees are warranted
20 under the circumstances.

1 **Over-recovery:** If the actual up-front financing costs are less than the
2 estimated costs, the Companies propose to credit the difference back to
3 customers through the semi-annual true-up mechanism discussed by
4 Companies witness Shana Angers, or in a manner otherwise determined
5 in the Financing Orders.

6 **Q. WHY DID THE COMPANIES PROPOSE ONE RECONCILIATION**
7 **METHOD IF AN UNDER-RECOVERY AND ANOTHER**
8 **RECONCILIATION METHOD IF AN OVER-RECOVERY?**

9 A. The Companies proposed different reconciliation methods based on the cash
10 flows involved in each situation. If there is an under-collection of up-front
11 financing costs, the Special Purpose Entity (“SPE”) will not have excess funds
12 to pay the difference. Therefore, DEC or DEP will be required to pay the
13 difference. As the amounts are not part of the bond principal amount, they will
14 not be collected through the storm recovery charge, but rather will need to be
15 recovered through a different mechanism by the impacted Company. By
16 contrast, if there is an over-collection of up-front financing costs, then the SPE
17 has received more funds from the bond issuance than what is needed to cover
18 the up-front financing costs, and these amounts will be factored into the next
19 true-up resulting in lower storm recovery charges for customers.

1 **Q. DOES THE PUBLIC STAFF AGREE WITH THE COMPANIES’**
2 **ACCOUNTING PROPOSAL FOR UNDER-RECOVERIES OF UP-**
3 **FRONT FINANCING COSTS?**

4 A. Yes. With respect to under-recoveries, the joint testimony of Public Staff
5 witnesses Michael C. Maness and Michelle M. Boswell states that the “Public
6 Staff does not oppose establishing a regulatory asset for prudently incurred and
7 properly accounted for under-recoveries of up-front costs.”² Public Staff
8 additionally recommends the regulatory asset be adjusted for income taxes and
9 accrued carrying costs at the Companies’ net-of-tax WACC return. The
10 Companies agree with this recommendation.

11 **Q. DOES THE PUBLIC STAFF AGREE WITH THE COMPANIES’**
12 **PROPOSAL FOR POTENTIAL OVER-RECOVERIES OF UP-FRONT**
13 **FINANCING COSTS?**

14 A. No. While the Companies propose to return this excess to customers in the next
15 storm charge true-up that will occur semi-annually, the Public Staff proposes
16 that any excess or over-collection be set aside in a regulatory liability, earning
17 a WACC return, to be considered in each Company’s next general rate case.

² Testimony of Michael C. Maness and Michelle M. Boswell Public Staff—North Carolina Utilities Commission, at 24, Docket Nos. E-2, Sub 1262 and E-7, Sub 1243 (filed Dec. 22, 2020).

1 **Q. ARE THE COMPANIES OPPOSED TO THE PUBLIC STAFF'S**
2 **RECOMMENDATION RELATED TO UNDER-RECOVERIES OF UP-**
3 **FRONT FINANCING COSTS?**

4 A. Yes. In addition to the reasons explained in witness Heath's testimony
5 regarding the separateness between the Companies and each SPE for
6 bankruptcy remoteness purposes, the Public Staff's proposal is a less efficient
7 and less practical method to returning these excess costs to customers than the
8 Companies' proposed methodology. Instead of recording a regulatory liability
9 and waiting to address the over-recovery in a subsequent rate case, the
10 Companies' method addresses the over-recovery through the semi-annual true-
11 up mechanism more quickly.

12 **B. On-Going Financing Costs**

13 **Q. PLEASE DESCRIBE THE PUBLIC STAFF'S PROPOSAL RELATED**
14 **TO ON-GOING FINANCING COSTS.**

15 A. As Companies witness Heath explains in his direct testimony, there will be on-
16 going expenses that will be incurred by each SPE throughout the life of the
17 storm recovery bonds to support its on-going operations. These on-going
18 financing costs include servicing fees; administration fees; accounting and
19 auditing fees; regulatory fees; legal fees; rating agency surveillance fees; trustee
20 fees; independent director or manager fees; and other miscellaneous fees
21 associated with the servicing of the storm recovery bonds.

1 The Public Staff makes recommendations in Public Staff witnesses
2 Maness and Boswell’s joint testimony, and mentioned in Public Staff
3 Consultant witness Paul Sutherland’s testimony, related to these on-going
4 financing costs that envision a future prudency review of such costs with the
5 Companies being required to create a regulatory liability for the purposes of
6 providing a credit to customers from the Companies for amounts determined to
7 be imprudently incurred.

8 **Q. DO THE COMPANIES AGREE WITH THE PUBLIC STAFF’S**
9 **RECOMMENDED ACCOUNTING TREATMENT FOR ON-GOING**
10 **FINANCING COSTS?**

11 A. No. For the reasons further explained in Companies witness Heath’s rebuttal
12 testimony, the Public Staff’s recommendation does not make practical sense
13 from a ratemaking perspective since the on-going financing costs are costs
14 incurred by the separate SPEs, not DEC or DEP. As such, allowing the Public
15 Staff to recommend adjustments to the Companies’ cost of service for costs the
16 Companies did not incur would be inappropriate. Additionally, while I’m not a
17 lawyer, based on my reading of N.C. Gen. § Stat. 62-172 (the “Securitization
18 Statute”), the Public Staff’s proposal expands the scope of the review permitted
19 by the Securitization Statute. Section (b)(3)d. of the Securitization Statute
20 clearly states, in plain language, that any review of an adjustment filing be
21 limited to mathematical and clerical errors, which is inconsistent with the Public

1 Staff's recommendation. Further, the Companies are not aware of any other
2 jurisdiction where this type of a mechanism is in place.

3 **Q. DOES THE PUBLIC STAFF MAKE A SIMILAR PROPOSAL**
4 **REGARDING THE COMPANIES' ACCOUNTING OF SERVICING**
5 **AND ADMINISTRATION FEES, WHICH QUALIFY AS ON-GOING**
6 **FINANCING COSTS?**

7 A. Yes. But before I continue, I want to highlight an important distinction between
8 including the servicing and administration fees in each Companies' cost of
9 service subject to a general rate case and other on-going financing costs. Unlike
10 other on-going financing costs, the servicing and administration fees are
11 collected *by* the Companies as payment for *their* services as servicer and
12 administrator, and the Companies are only entitled to earn a fee for the
13 incremental costs incurred in servicing bonds and administering their applicable
14 SPE. Therefore, it is entirely appropriate to include those fees in the
15 Companies' respective cost of service because these are fees received by the
16 Companies, not the SPEs. Accordingly, the Companies recommended that the
17 fees would be reflected in future rate case cost of service studies, so the
18 Companies are only compensated for the incremental costs incurred in
19 connection with performing their obligations under the servicing and
20 administration agreements.

21 However, the Public Staff recommends that since general rate case
22 proceedings do not occur every year, these servicing and administrative fees

1 should be tracked separately and any over-collections should be held in a
2 regulatory liability account to be refunded to customers in the next general rate
3 case, adjusted for income taxes and accrued carrying costs at the Companies'
4 net-of-tax WACC.

5 **Q. DO THE COMPANIES AGREE WITH THE PUBLIC STAFF'S**
6 **RECOMMENDED TREATMENT?**

7 A. No. The Companies believe the servicing and administration fees are
8 reasonable and tracking of the actual costs incurred is unnecessary, given the
9 magnitude of the dollars involved. The servicing and administration fees are
10 estimated to be approximately \$180,000 per year for DEC and approximately
11 \$460,000 per year for DEP. Therefore, the difference between these payments
12 received by the utilities and the actual costs incurred is likely to be even smaller.
13 Amounts of this magnitude, well under a million dollars for DEC and DEP
14 combined, are not typically considered material enough to establish regulatory
15 assets and liabilities and track outside of a general rate case. Moreover, the
16 administrative effort to track these costs in the way the Public Staff suggests
17 will increase costs to customers without providing any material benefit. The
18 Companies' proposal instead produces a similar result using less burdensome
19 and more efficient means.

1 **C. Tail-End Collections**

2 **Q. PLEASE SUMMARIZE THE COMPANIES' INITIAL PROPOSAL AS IT**
3 **RELATES TO POTENTIAL OVER-RECOVERIES OF TAIL-END**
4 **COLLECTIONS.**

5 A. Overcollection related to tail-end collections is due to the timing difference of
6 when billing and collections cease, and the storm recovery bonds are fully
7 recovered. The Companies proposed that any overcollection would be recorded
8 to a regulatory liability account for any amounts remaining in each Collection
9 Account, less the amount of any Capital Subaccount, which would be credited
10 back to customers in the next general rate case following the maturity of the
11 storms recovery bonds.

12 **Q. DOES THE PUBLIC STAFF AGREE WITH THE COMPANIES'**
13 **PROPOSAL RELATING TO TAIL-END COLLECTIONS.**

14 A. The Public Staff's recommendation agrees in part with the Companies that the
15 tail-end collections should be recorded to a regulatory liability; however, Public
16 Staff additionally recommends the regulatory liability be adjusted for income
17 taxes and accrued carrying costs at the Companies' net-of-tax WACC.

18 **Q. DO THE COMPANIES AGREE WITH THE PUBLIC STAFF'S**
19 **ADDITIONAL PROPOSAL RELATING TO TAIL-END**
20 **COLLECTIONS?**

21 A. Yes, the Companies agree with this methodology. The tail-end collections will
22 stay with the SPE trustee until the storm recovery charge is set at \$0 and no

1 more cash from the storm recovery charge is being collected. At that point in
2 time, all cash at the trustee (i.e. the Excess Funds and Capital Subaccounts) will
3 be distributed to DEC and DEP. Once the cash from the tail-end collections is
4 received by DEC and DEP, the regulatory liability discussed above would be
5 recorded. Until DEC and DEP actually receive the cash from the SPE trustee,
6 there is no actual liability to customers.

7 **Q. DO YOU HAVE ANY COMMENTS ON THE RECOMMENDATION**
8 **PROPOSED BY THE PUBLIC STAFF RELATED TO THE**
9 **COMPANIES' INITIAL CAPITAL CONTRIBUTION TO THE SPE, IN**
10 **LIGHT OF THE PROPOSED TREATMENT OF TAIL-END**
11 **COLLECTIONS?**

12 A. Yes. While Companies witness Heath addresses the Public Staff's
13 recommended return on the Companies' capital contribution in his rebuttal
14 testimony, one related observation I would like to make is that Public Staff's
15 recommendation of a WACC return on the regulatory liability related to
16 potential tail-end collections is inconsistent with their recommendation related
17 to the return on the Companies' capital contributions. In both scenarios, funds
18 have been contributed by an entity (the customers in the event of any tail-end
19 collections and the Companies for the initial capital contribution) and held for
20 a period of time (15 to 20 years in the case of the initial contributions, and the
21 period between the end of the storm recovery charge and the next general rate
22 case for the tail end collections), and so a reasonable return to reimburse the

1 entity for the cost of using those funds for that period should be awarded.
2 However, unlike the tail-end collections, the Public Staff has recommended that
3 the return on the capital contributions be limited to only the investment return
4 on the funds while the Companies have proposed to earn a return at the interest
5 rate of the highest tranche of bonds, which is actually less than their WACC.
6 Similar to traditional utility capital expenditures, the capital contributions are
7 amounts borrowed from the Companies' investors and provided to the SPEs,
8 and the Companies will incur costs for the use of those funds for the duration
9 of the bond period and have proposed to earn a return at the interest rate of the
10 highest tranche of bonds, even though their WACC, which again is higher, is
11 actually the true cost the Companies will incur for the use of the funds.
12 Accordingly, to further discount this amount would be inappropriate. The
13 Public Staff and their consultant reference benefits to the Company from
14 securitization and use this as a justification to deny full cost recovery. While
15 we disagree with the use of this justification, even if that were the case,
16 customers are also quantifiably benefitting from the securitization as shown in
17 my exhibits, but yet the Public Staff is recommending the use of the Companies'
18 WACC as the appropriate level of return that customers should receive, which
19 exposes the asymmetry of the Public Staff's argument. While it is hard to
20 predict the timing of rate cases after conclusion of the storm recovery charge, it
21 is likely that it will be less than the 15 to 20 years that the Companies will not
22 have access to the capital contributions, which in my opinion is another

1 argument for a more similar return. Again, the Companies agree with the
2 application of the WACC to the tail-end collections but are seeking somewhat
3 symmetrical treatment for their contribution.

4 **III. CALCULATION OF QUANTIFIABLE CUSTOMER BENEFITS**

5 **Q. ARE THERE ISSUES RAISED BY THE PUBLIC STAFF'S**
6 **CONSULTANT THAT YOU WOULD LIKE TO ADDRESS**
7 **REGARDING THE CALCULATION OF QUANTIFIABLE**
8 **CUSTOMER BENEFITS?**

9 A. Yes. I would also like to address comments by Public Staff Consultant witness
10 Sutherland regarding the interest rate used in the net present value calculation
11 of quantifiable benefits to customers for both Companies. Witness Sutherland
12 argues that the interest rate used in the calculation of quantifiable benefits to
13 customers results in an overstatement of savings, and also argues that there was
14 an error in the estimate of the A-5 tranche interest rate that was provided by
15 Companies witness Charles N. Atkins II, thus impacting the weighted average
16 interest rate. Companies witness Atkins will address the comments around the
17 interest rates used in the models and I will respond to the comments around the
18 interest rate used in the quantifiable benefits calculation.

1 **Q. DO YOU AGREE WITH WITNESS SUTHERLAND'S**
2 **CHARACTERIZATION OF THE BOND INTEREST RATE USED IN**
3 **EXHIBIT 7 AS AN "ERROR"?**

4 A. No. The calculations of quantifiable benefits for DEC and DEP provided in
5 Abernathy Exhibits 5-7 were based on a high-level model that was developed
6 by the Companies and the Public Staff during negotiations that led to the First
7 Partial Stipulations in the Companies' recently concluded rate cases, Docket
8 Nos. E-7, Sub 1214 and E-2, Sub 1219. This model included several
9 assumptions related to storm dates, dates of rate cases, timing of securitization,
10 interest rates, and financing costs to be used in the hypothetical savings
11 calculation based on the First Partial Stipulations. Accordingly, I agree that the
12 interest rate used in Abernathy Exhibit 7 is not representative of the average
13 interest rate over the life of the bonds being considered in this transaction, as
14 discussed by witness Sutherland. The rates used are the weighted average rate
15 at issuance of the bonds, based on the principal amount of each tranche, but this
16 rate is just used as an assumption for a bond interest rate in the high-level
17 savings model.

18 In fact, in my direct testimony, I acknowledged that the high-level model
19 included various assumptions around dates of the Storms and new rates'
20 effective dates in the pending rate cases. I also noted that if the actual dates had
21 been used in the analysis of savings then, the revenue requirement would have
22 increased, but the comparison of the Traditional Recovery Model and the Storm

1 Securitization Model would still show savings. Public Staff witnesses Maness
2 and Boswell even acknowledged on page 27 of their testimony that the high-
3 level model I used incorporated the assumptions agreed to by the Companies
4 and the Public Staff in their First Partial Stipulations. If Public Staff
5 Consultants believe a more precise interest rate should now be used in the
6 customer benefit calculation, then it is appropriate to also adjust other
7 assumptions, including using actual dates related to Storms and new rates'
8 effective dates, as well as using the actual estimated cash flows from the Storm
9 Securitization Model. As such, I have recalculated the quantifiable benefits to
10 factor in the actual date of the Storms, the dates of interim rates effective in the
11 pending rate cases, and the actual estimated cash flows from securitization as
12 shown in Abernathy Rebuttal Exhibit 4. The actual cash flows from the Storm
13 Securitization Model reflect the more precise weighted interest cost over time
14 referenced by witness Sutherland.

15 Consistent with the First Partial Stipulations, the calculations assume up
16 to 12 months of amortization expense and capital costs were excluded from the
17 revenue requirement for the Traditional Recovery Model. The revised
18 calculation for the Traditional Recovery Model is included as Abernathy
19 Rebuttal Exhibit 2 for each Company. The revised calculation for the Storm
20 Securitization Model, based on actual estimated cash flows, is included as
21 Abernathy Rebuttal Exhibit 3 for each Company. The revised net present value

1 comparison for quantifiable customer benefits is shown as Abernathy Rebuttal
2 Exhibit 1 for each Company.

3 **Q. WHAT ARE THE CUSTOMER SAVINGS AMOUNTS FOR DEC AND**
4 **DEP BASED ON ACTUAL DATES AND ESTIMATED CASH FLOWS**
5 **ASSUMING A 15-YEAR BOND PERIOD?**

6 A. The updated calculations are provided in Abernathy Rebuttal Exhibits 1-3 for
7 each Company. Based on these calculations, DEC expects approximately \$57.5
8 million, or 31.2%, in customer savings will be achieved through securitization
9 of its storm costs, as compared to \$58 million, or 32% noted in the Joint
10 Petition. Similarly, DEP expects approximately \$216.2 million, or 34.4%, in
11 customers savings will be achieved through securitization of its storm costs, as
12 compared to \$199 million, or 33% noted in the Joint Petition. In summary,
13 regardless of the calculation used, the Companies anticipate significant
14 customer benefits being achieved through securitization.

15 **IV. 15- OR UP TO 20-YEAR BOND AMORTIZATION PERIOD**

16 **Q. WHAT BOND AMORTIZATION PERIOD DID THE COMPANIES**
17 **PROPOSE?**

18 A. The Companies proposed a 15-year amortization period.

19 **Q. ARE THE COMPANIES OPPOSED TO THE PUBLIC STAFF'S 20-**
20 **YEAR BOND AMORTIZATION PERIOD PROPOSAL?**

21 A. No, if lengthening the amortization is desirable to the Commission under the
22 circumstances. However, for the reasons stated in witness Heath's direct

1 testimony³, the Companies continue to support their original 15-year
2 amortization period as a reasonable and appropriate balance between customer
3 benefits and the length of the bonds and associated storm recovery charge.
4 Additionally, I agree with the “note of caution” raised by Public Staff witnesses
5 Maness and Boswell on page 28 of their joint testimony concerning long term
6 amortization periods, and believe this Public Staff statement evidences the
7 reasonableness of the Companies’ original 15-year proposal.

8 **Q. PLEASE PROVIDE THE CALCULATION OF QUANTIFIABLE**
9 **CUSTOMER BENEFITS IF A 20-YEAR BOND AMORTIZATION**
10 **PERIOD IS USED FOR THIS SECURITIZATION.**

11 A. The calculation of quantifiable customer benefits assuming a 20-year bond
12 amortization period is shown in Abernathy Rebuttal Exhibits 4 and 5 for both
13 DEC and DEP. A 20-year bond term is estimated to provide approximately
14 \$67.9 million (36.9%) savings to customers for DEC and \$249.8 million
15 (39.8%) savings to customers for DEP. The calculation uses the actual
16 estimated cash flows for a 20-year bond structure as provided by Companies
17 witness Atkins. For the Traditional Recovery Model, the revenue requirement
18 remains the same as in Abernathy Rebuttal Exhibit 2 for each Company, given
19 that 15 years was the longest recovery period proposed in the rate cases.

³ Direct Testimony of Thomas J. Heath, Jr., at 8-9, Docket Nos. E-7, Sub 1243 and E-2, Sub 1262 (Oct. 26, 2020).

1 **V. PUBLIC STAFF ADDITIONAL AUDIT OF STORM COSTS**

2 **Q. PLEASE SUMMARIZE THE PUBLIC STAFF’S REQUEST FOR AN**
3 **ADDITIONAL AUDIT OF THE COMPANIES’ STORM COSTS.**

4 A. The Public Staff requests that the Commission require the Companies to
5 provide “any further supporting documentation [of O&M expenses since the
6 general rate cases] requested by the Public Staff” to perform an additional audit
7 of the Companies’ storm costs.

8 **Q. WHAT IS THE PUBLIC STAFF’S REASONING FOR THIS**
9 **ADDITIONAL AUDIT?**

10 A. Public Staff witnesses Maness and Boswell state that the “Public Staff has not
11 been able to fully review all the changes in recorded O&M expenses since the
12 general rate cases,” and that, therefore, those changes in expenses remain
13 subject to future review, including a prudence review in a future general rate
14 case.

15 **Q. WAS THE PUBLIC STAFF GRANTED AN OPPORTUNITY TO**
16 **REVIEW THESE COSTS DURING THE RATE CASE AND THIS**
17 **DOCKET’S DISCOVERY PERIOD?**

18 A. Yes. Since the completion of the Public Staff’s investigation into the
19 Companies’ proposed retail electric rates and charges in their respective general
20 rate case dockets (in which the vast majority of the underlying storm costs were
21 audited and determined by the Public Staff to be reasonably and prudently

1 incurred)⁴, the Public Staff had nearly two months to conduct an audit of any
 2 adjustments to storm costs.⁵ As witnesses Maness and Boswell admit on page
 3 10 of their testimony, the Public Staff already had supporting documentation
 4 for the net reduction in costs in their possession. Notwithstanding, the Public
 5 Staff only asked one follow-up question regarding the underlying storm costs
 6 during the discovery period (*see* Heath Exhibit 1, Public Staff Data Request No.
 7 11-3).

8 **Q. DO THE COMPANIES AGREE WITH THE RECOMMENDATIONS OF**
 9 **PUBLIC STAFF WITNESSES MANESS AND BOSWELL REGARDING**
 10 **FURTHER AUDITS OF THE UNDERLYING STORM RECOVERY**
 11 **COSTS?**

12 A. The Companies completely understand and support the Public Staff's general
 13 need and authority to audit the Companies' costs. However, the Companies do
 14 not agree with the Public Staff's request in this case due to timing and the need
 15 for certainty coming out of this proceeding of the underlying storm costs
 16 eligible for securitization. The amounts included in the rate cases included
 17 estimates of storm costs as the amounts were being finalized and the Public
 18 Staff determined that the amounts included in the rate cases were reasonable
 19 and prudently incurred. Since the rate cases, the storm costs have been finalized

⁴ Public Staff witnesses Maness and Boswell acknowledge on page 9 of their joint testimony that the Companies updated the amounts of the O&M storm expenses in their respective rate cases.

⁵ The Companies filed their storm securitization petition on October 26, 2020. Discovery on the Companies' petition ended on December 15, 2020. The Public Staff's first set of discovery requests was submitted on October 23, 2020, which is three days prior to the Companies' actual filing. The Public Staff clearly knows how and when to issue discovery on matters it wishes to explore.

1 and the amount of storm costs *decreased* from the amount included in the rate
2 cases to the amount included in the Joint Petition. The Companies' storm costs
3 have not changed since they filed their Joint Petition in October 2020 and the
4 Public Staff had ample opportunity to audit the post rate case adjustments
5 during the discovery period established in this proceeding but did not do so.
6 The Public Staff should not now be afforded the opportunity to go back, at this
7 late stage, to audit the post rate case adjustments, which decreased the costs
8 included in the rate cases. To successfully structure, market, and price these
9 bonds, the Companies need certainty regarding the underlying storm costs
10 eligible for securitization. The Companies will not have that certainty if the
11 underlying storm costs, which have been static for months, remain subject to
12 audit for an indefinite period by the Public Staff. In the Companies' opinion,
13 the over-riding need for certainty on securitized costs outweighs the marginal
14 benefit to regulatory certainty that might be gained by a future audit of a very
15 small portion of the storm costs being securitized in these circumstances. For
16 these reasons, the Commission should deny the Public Staff's request.

17 **VI. CONCLUSION**

18 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

19 A. Yes.

1 MR. ROBINSON: Thank you,
2 Chair Mitchell.

3 Q. Ms. Abernathy, do you have a summary of your
4 testimony?

5 A. Yes, I do.

6 Q. Would you please provide that summary to the
7 Commission.

8 A. Sure. Good morning. My name is
9 Melissa Abernathy, and I'm a director of rates and
10 regulatory planning for North and South Carolina
11 representing both Duke Energy Carolinas and Duke Energy
12 Progress. I am pleased to appear before you today to
13 discuss various aspects of the proposed storm
14 securitization transaction which will provide
15 significant quantifiable benefits to customers.

16 My direct testimony supports the revenue
17 requirement calculations for the storm recovery charges
18 resulting from the Companies' proposal to use storm
19 recovery bonds to finance the incremental O&M and
20 capital investments related to Hurricanes Florence,
21 Michael, Dorian, and Winter Storm Diego, as well as
22 accrued carrying charges as permitted by the
23 securitization statute.

24 The revenue requirements are designed to

1 repay the proposed storm recovery bonds as well as all
2 upfront and ongoing financing costs associated with the
3 securitization bond structure. Within my testimony, I
4 demonstrate the quantifiable benefits that customers
5 receive through a storm bond issuance as compared to
6 the traditional recovery model.

7 The magnitude of the 2018 and 2019 storm was
8 unprecedented in the Companies' service territories
9 resulting in the Companies collectively financing
10 approximately \$1 billion in storm recovery costs and
11 associated carrying charges. These storms and their
12 costs have been outlined extensively in the current
13 pending rate case dockets and in the associated storm
14 deferral dockets that preceded the rate cases.

15 The storm discovery costs were updated in
16 this docket to include final costs incurred related to
17 the storms, which resulted in an overall decrease in
18 the amount of storm costs from what was presented in
19 the rate case. The Public Staff previously reviewed
20 the storm costs originally included in the rate cases
21 and found them to be reasonable and prudently incurred.
22 The Companies and the Public Staff agreed on pursuing
23 securitization of these storm costs as outlined in the
24 securitization statute and agreed upon certain

1 assumptions to be used in the calculation of
2 quantifiable benefits to customers.

3 As noted in my rebuttal testimony, over a
4 15-year bond period, Duke Energy Carolinas expects
5 securitization to provide an approximate \$58 million or
6 31 percent net present value benefit to customers when
7 compared to traditional recovery mechanisms, while DEP
8 expects securitization to provide an approximate
9 \$216 million or 34 percent net present value benefit to
10 customers when compared to traditional recovery
11 mechanisms.

12 The primary purpose of my rebuttal testimony
13 is to respond to comments from Public Staff witnesses
14 related to accounting and auditing of the storm costs
15 and financing costs associated with the transaction.
16 Public Staff's testimony included accounting
17 recommendations to track and audit the various upfront
18 and ongoing financing costs that are required by each
19 company's separate special purpose entity, as well as
20 comments related to the servicing and administration
21 fees received by each company from its respective SPE.
22 However, it's my understanding that the Companies and
23 the Public Staff have reached a settlement agreement
24 regarding the accounting issues addressed in my

1 rebuttal testimony. I am happy to answer any questions
2 the Commission may have on the settlement and
3 agreements reached therein regarding the accounting of
4 the storm recovery costs and financing costs.

5 In summary, Duke Energy has earned a
6 consistent and strong reputation within the industry
7 for our rapid and capable response to these extreme
8 weather events in North Carolina. The Companies and
9 the Commission have an opportunity to use the recently
10 passed securitizations statute to provide significant
11 benefits to customers as well as create a structure in
12 which the Company is able to recover its storm costs
13 quickly and efficiently.

14 Q. Thank you, Ms. Abernathy.

15 MR. ROBINSON: Chair Mitchell, the
16 witness is available for questions.

17 MR. GRANTMYRE: I have one cross
18 examination, a very harmless question. I know I
19 didn't list it, but.

20 CROSS EXAMINATION BY MR. GRANTMYRE:

21 Q. Ms. Abernathy, would you agree that the Duke
22 and the Public Staff had extensive negotiations to come
23 into this settlement, and the persons on the Public
24 Staff side were Mike Maness and Michelle Boswell that

1 will testify later, and there was a lot of
2 give-and-take?

3 A. I would agree with that.

4 Q. Thank you. That's all I have.

5 CHAIR MITCHELL: Mr. Grantmyre, just so
6 I'm clear, is that all from the Public Staff for
7 this witness?

8 MR. GRANTMYRE: Yes. That's all we
9 have. Thank you.

10 CHAIR MITCHELL: Okay. So,
11 Mr. Grantmyre, I heard you say yes, that's all from
12 the Public Staff for the witness. All right.

13 CIGFUR, anything for this witness?

14 MS. CRESS: Nothing for this witness.
15 Thank you, Chair Mitchell.

16 CHAIR MITCHELL: Okay. All right.
17 Mr. Robinson, any redirect on the question?

18 MR. ROBINSON: No redirect,
19 Chair Mitchell.

20 CHAIR MITCHELL: Okay. All right. I
21 will turn to my colleagues to see if there are any
22 questions from Commissioners.

23 Commissioner Brown-Bland?

24 COMMISSIONER BROWN-BLAND:

1 Chair Mitchell, I have no questions.

2 CHAIR MITCHELL: All right.

3 Commissioner Gray?

4 COMMISSIONER GRAY: No questions.

5 CHAIR MITCHELL: Commissioner

6 Clodfelter?

7 COMMISSIONER CLODFELTER: Nothing.

8 CHAIR MITCHELL: Okay.

9 Commissioner Duffley?

10 COMMISSIONER DUFFLEY: I have no
11 questions.

12 CHAIR MITCHELL: Commissioner Hughes?

13 COMMISSIONER HUGHES: No questions for
14 me.

15 CHAIR MITCHELL: All right.

16 Commissioner McKissick?

17 COMMISSIONER MCKISSICK: No questions.

18 CHAIR MITCHELL: All right.

19 Ms. Abernathy, you almost got off pretty easily,
20 but I have some questions for you.

21 EXAMINATION BY CHAIR MITCHELL:

22 Q. I'm not sure if you heard the question I
23 posed to Mr. Atkins yesterday, and I should have -- I
24 should have held the question for you. But we're

1 interested in the audit that you-all have agreed to
2 with the Public Staff and the settlement agreement that
3 was filed on the 27th.

4 What is your understanding of the scope of
5 the audit that will be performed on the ongoing
6 financing costs that are incurred associated with these
7 issuances?

8 A. Yes. My understanding of the scope of the
9 audit is that it allows the Public Staff to audit for
10 clerical and mathematical accuracy as we include those
11 actual ongoing costs into the true-up mechanism, as
12 well as to audit for charges that may be the result of
13 recklessness, wilful misconduct, or gross negligence of
14 the Companies or the SPE.

15 Q. Okay. So is that -- just so I'm clear, is
16 that a less rigorous analysis or a more restrictive
17 scope of analysis than would typically be done under a
18 prudency review-type analysis?

19 A. I would say that standard is less than the
20 standard of a prudency review that's typically applied
21 to traditional utility costs that go through
22 traditional ratemaking.

23 Q. Okay. And can you help us understand why
24 it's necessary to have a more limited scope here on

1 these costs --

2 A. Sure.

3 Q. -- than a prudency review? Just so my
4 question is clear.

5 A. Yeah, sure. So I think it's good to
6 understand the difference between the traditional
7 utility costs and then what these costs represent. So
8 in traditional ratemaking for traditional utility
9 costs, those are subject to prudence review, and in
10 return, the Companies are allowed to earn a return at
11 the weighted average cost of capital through that
12 structure.

13 The standard of review here for these ongoing
14 costs is different just because the structure of
15 recovery is different through securitization. So these
16 costs are different than traditional utility costs.
17 These are the costs of the SPE in order to -- and
18 they're required in order to issue the storm recovery
19 bonds. And Company witness Atkins went through the
20 various reasons why it's important for the SPE to
21 remain whole for their ongoing financing costs and the
22 reason that it's structured that way to support the
23 structure of the bonds. And it's important that that
24 structure is maintained so that we could pass savings

1 on and achieve the lower costs through storm
2 securitization statute.

3 And so with regards to the audit that we
4 agreed to in the settlement, the storm securitization
5 statute allows for your mathematical and clerical
6 errors through the true-up mechanism process, and
7 that's consistent with the storm securitization
8 statute. And then this audit is also an audit to
9 ensure no charges are a result of recklessness, wilful
10 misconduct, and gross negligence, which is in line with
11 the requirements of the servicing and administration
12 agreements of the Company.

13 But in summary, it's there to support the
14 structure of this transaction, which is different than
15 traditional recovery.

16 Q. Okay. Okay. That's helpful. I appreciate
17 that response. Another question that we have for
18 you-all -- we'll pose the same question to the Public
19 Staff -- and if you want the appropriate witness to
20 respond to the question, just let me know.

21 But the -- as we understand, you know, the
22 proposal, the storm costs will accrue interest or -- at
23 the weighted average cost of capital up to and until --
24 the weighted average cost of capital established in the

1 Companies' 2017 rate cases, and then at some point in
2 time will accrue interest at the weighted average cost
3 of capital at that which is approved in the current or
4 the 2019 -- it's what we're referring to them as, I
5 guess -- the 2019 rate cases.

6 So is -- can you help me understand what
7 that -- what the Company sees as that specific point in
8 time when the transition will occur from one weighted
9 average cost of capital to the next? And how -- so
10 that's my first question. And my second question are
11 the mechanics of that. I mean, it's going to
12 necessarily cause an adjustment in the cost to be
13 securitized, so how will that adjustment occur and at
14 what point in the securitization process will that
15 occur?

16 A. Sure. So, to your first question, we will
17 accrue carrying charges at the recently approved
18 weighted average cost of capital from the last rate
19 case up until we implement -- up until we implement
20 rates in this rate case. And so we have implemented
21 interim rates associated with these rate cases. And
22 so, at that point, we -- when we implemented the
23 interim rates, it was based on the second partial
24 settlement in the rate cases, and we began to accrue

1 carrying charges at that level.

2 Q. Okay. So since those interim rates are
3 already in effect, is the response, then, that the
4 Company -- that these costs would already be accruing
5 carrying charges at that interim weighted average cost
6 of capital?

7 A. Yes.

8 Q. Okay. Okay. Thank you.

9 A. And if in the final order something needs to
10 change, we would adjust those calculations to reflect
11 the accrued weighted average cost of capital approved
12 in this rate case.

13 Q. Okay. And can that adjustment be affected
14 such that the actual storm costs that are securitized
15 reflect the adjustment, or will the adjustment have to
16 be flowed through one of the mechanisms outside of the
17 actual securitized storm costs? Does that question
18 make sense?

19 A. Yes. It will be adjusted as part of the IAL
20 process prior to issuance of the bond.

21 Q. Got it.

22 A. So all of our assumptions around carrying
23 costs, the date of the issuance of the bond, all of
24 that will be updated so that, through the IAL process,

1 there will be a final calculation of what the actual
2 storm recovery charges are that will be covered through
3 these bonds.

4 Q. Okay. I got it. That clears it up for me.
5 Okay. All right. That's it for me for you,
6 Ms. Abernathy. I appreciate your responses to my
7 questions.

8 CHAIR MITCHELL: I will check in with
9 counsel to see if they have questions on any of my
10 questions.

11 MR. GRANTMYRE: Public Staff has none.

12 CHAIR MITCHELL: Okay. Thank you,
13 Mr. Grantmyre.

14 Mr. Robinson?

15 MR. ROBINSON: Chair Mitchell, no
16 questions based off of your particular questions.
17 I would just make a comment, though. Ms. Abernathy
18 is our accountant witness, and I understand that
19 Commissioner Clodfelter asked some questions about
20 why we did not include a storm recovery reserve in
21 this docket. If counsel does not object, I would
22 like to give Ms. Abernathy, our accounting witness,
23 an opportunity to respond to that question. But,
24 again, that's if counsel does not object.

1 MR. GRANTMYRE: We do not object.

2 MS. CRESS: No objection for the CIGFUR.

3 CHAIR MITCHELL: Okay. All right.

4 Ms. Abernathy, you may proceed.

5 THE WITNESS: Okay. So as the
6 Commission is aware, the costs related to these
7 storms were included -- were originally included in
8 our original storm referral dockets and then
9 consolidated into the pending rate cases. And as
10 part of the first partial settlement in those
11 pending rate cases, the Companies and Public Staff
12 agreed to remove those costs from the rate cases to
13 pursue securitization under the securitization
14 statute.

15 And so we are using this transaction to
16 do just that, to pursue securitization of those
17 costs. And we opted not to add in a storm reserve
18 just to not overly complicate this transaction, but
19 we would be open to a storm reserve.

20 CHAIR MITCHELL: Okay. Thank you,
21 Ms. Abernathy. And I realize, Mr. Robinson, I have
22 more one question for your witness, so I'm going to
23 ask my question, then we'll go back through to see
24 if there are any questions on this question.

1 Q. This is a question from the Commission staff,
2 Ms. Abernathy, so I'm gonna read it, so just bear with
3 me. I want to make sure I get their question answered.
4 All right. So I assume you have your direct testimony
5 in front of you. And you may not need to reference it,
6 but just have it on hand in case you need to refer back
7 to it.

8 But on page 9 of your direct, lines 13
9 through 16, in response to the question of whether the
10 costs contained in DEC and DEP's storm recovery costs
11 meet the definition of storm recovery costs pursuant to
12 the statute, you state as follows:

13 "Finally, the costs eligible for recovery
14 pursuant to the securitization statute there
15 included in the storm recovery cost are
16 reduced by the highest amount within the
17 normal range of fluctuation included in each
18 Company's 2019 rate case at the time of the
19 storms."

20 So here's the question: Can you explain
21 exactly what is meant by this statement and provide an
22 example of the reduction in the costs eligible for
23 recovery with respect to the present dockets?

24 A. Yes. So the level of costs that are

1 recovered related to storm recovery activities is set
2 through each rate case. And there's two different
3 numbers that are looked at. There's one, there's the
4 average storm costs in the last 10 years, and that's
5 the average year -- the average of storm costs in the
6 last few years sets the level that's included in rates,
7 and then that's reviewed and approved in a rate case.

8 This normal range of storms is -- the way we
9 look at that is the largest year within the 10-year
10 average. And so that's recognizing the fact that some
11 years may have more storm costs than the average and
12 some may have less, and so we look at that normal storm
13 range before we consider whether there's costs to defer
14 in a given year for significant storms.

15 And so in this case, I may not have the
16 specific details of which storm, but for each year, we
17 looked at the storms and what year they were incurred
18 in, where we were in line with that normal storm range,
19 and the amounts we are proposing for recovery and the
20 amounts that are above that amount. And those
21 calculations have been included in our -- within the
22 rate case and have been reviewed by the Public Staff.

23 Q. Okay. Thank you very much for that
24 explanation. All right.

1 CHAIR MITCHELL: Questions from counsel
2 on my question.

3 Mr. Grantmyre?

4 MR. GRANTMYRE: Public Staff has none.

5 CHAIR MITCHELL: Okay. Ms. Cress?

6 MS. CRESS: CIGFUR has none. And my
7 apologies, I was made aware that my camera was not
8 turned on earlier when I was speaking. My bad.

9 CHAIR MITCHELL: Okay. We see you now.
10 All right.

11 Mr. Robinson?

12 MR. ROBINSON: No questions.

13 CHAIR MITCHELL: Okay. All right.
14 Well, Ms. Abernathy, it appears that you have come
15 to the end of your appearance before us. Counsel,
16 I'll entertain -- or, Mr. Robinson, I'll entertain
17 a motion.

18 MR. ROBINSON: Thank you,
19 Chair Mitchell. At this time, obviously, the
20 Companies ensure that the witness' testimony and
21 exhibits are moved into the record, and at this
22 time, we would reserve the right to call
23 Ms. Abernathy in the event that she is needed.

24 CHAIR MITCHELL: Okay. Well,

1 Ms. Abernathy, I may have spoken too soon. You are
2 subject to recall, so you may step down for now
3 subject to that recall.

4 And, Mr. Robinson, hearing no objection
5 to your motion, the exhibits to Ms. Abernathy's
6 testimony will be admitted into evidence.

7 (Abernathy DEC Exhibits 1 through 7,
8 Abernathy DEP Exhibits 1 through 7,
9 Abernathy DEC Rebuttal Exhibits 1
10 through 5, and Abernathy DEP Rebuttal
11 Exhibits 1 through 5, were admitted into
12 evidence.)

13 THE WITNESS: Thank you.

14 CHAIR MITCHELL: All right. With that,
15 you may step down, Ms. Abernathy. And,
16 Mr. Robinson, you may call your next witness.

17 MR. ROBINSON: Thank you,
18 Chair Mitchell. The Company is pleased to state
19 that it has ended its direct case -- direct and
20 rebuttal case, frankly. And so, at this time, I
21 believe the only lingering motions out there is the
22 testimony and exhibits of excused witnesses
23 Jonathan Byrd and Shana Angers. At this time, we
24 would move that those testimony for those two

1 witnesses and exhibits be moved into the record.

2 CHAIR MITCHELL: All right. Hearing no
3 objection to that motion, Mr. Robinson, the
4 testimony and exhibits of Company witnesses Byrd
5 and Angers shall be -- Angers -- I'm sorry, I
6 apologize -- Angers shall be accepted into
7 evidence.

8 (Byrd DEC Exhibits 1 and 2, Byrd DEP
9 Exhibits 1 and 2, and Angers Exhibits 1
10 and 2, were admitted into evidence.)

11 (Whereupon, the prefiled direct
12 testimony of Jonathan L. Byrd and the
13 prefiled direct testimony of
14 Shana W. Angers were copied into the
15 record as if given orally from the
16 stand.)

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BEFORE THE NORTH CAROLINA UTILITIES COMMISSION**DOCKET NO. E-7, SUB 1243
DOCKET NO. E-2, SUB 1262**

In the Matter of:)	
	)	DIRECT TESTIMONY OF
Petition of Duke Energy Carolinas, LLC	)	JONATHAN BYRD
And Duke Energy Progress, LLC for	)	FOR DUKE ENERGY
Issuance of Storm Cost Recovery Financing	)	CAROLINAS, LLC AND DUKE
Orders	)	ENERGY PROGRESS, LLC

1 **I. INTRODUCTION**

2 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

3 A. My name is Jonathan Byrd, and my business address is 550 South Tryon Street,
4 Charlotte, North Carolina.

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

6 A. I am Director, Southeast Pricing & Regulatory Solutions for Duke Energy
7 Carolinas, LLC (“DEC”), Duke Energy Progress, LLC (“DEP”), and Duke
8 Energy Florida, LLC, testifying on behalf of DEC and DEP (each a “Company”
9 or collectively “the Companies”).

10 **Q. PLEASE BRIEFLY SUMMARIZE YOUR EDUCATIONAL
11 BACKGROUND AND PROFESSIONAL EXPERIENCE.**

12 A. I received a Bachelor of Science degree in Mechanical Engineering from the
13 University of North Carolina (“UNC”) at Charlotte, a Master of Engineering
14 degree from NC State University, and a Master of Business Administration
15 degree from UNC-Chapel Hill.

16 I joined Duke Energy Corporation in 2005 and have worked in various
17 roles providing products and services to large business customers, corporate
18 finance and renewable energy. In June of 2020 I moved into my current role in
19 Pricing and Regulatory Strategy.

20 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE NORTH
21 CAROLINA UTILITIES COMMISSION (“COMMISSION”)?**

22 A. Yes. I have testified previously, including in Docket No. E-7, Sub 1052,
23 regarding DEC’s 2013 REPS compliance report and application for approval of

1 its REPS cost recovery rider, and in Docket No. E-2, Sub 1043, regarding
2 DEP's 2014 application for approval of its REPS cost recovery rider.

3 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

4 A. My testimony demonstrates that the storm recovery charge rates each Company
5 proposes reflect appropriate rate making principles and result in an equitable
6 basis for recovery of each Company's revenue requirements across and within
7 their respective customer classes and rate schedules. My testimony: (1)
8 describes the changes to each Company's retail electric rate schedules; (2)
9 quantifies the effect of these proposed changes on each Company's North
10 Carolina retail electric customers; (3) discusses how each Company proposes
11 to implement the storm recovery charges, as quantified in witness Melissa
12 Abernathy's testimony; and (4) describes other requested changes to each
13 Company's tariff.

14 **Q. WHAT IS THE SCOPE OF YOUR TESTIMONY?**

15 A. My testimony is principally devoted to outlining the steps followed in
16 calculating the proposed storm recovery charge by rate class for each Company.
17 While the final storm recovery charges by rate class will not be calculated until
18 after the final terms of the issuance of storm recovery bonds have been
19 established, my testimony outlines the methodology that will be used in
20 developing the proposed storm recovery charges. Barring significant changes
21 in the terms of an issuance of storm recovery bonds, or significant changes in
22 embedded benchmark interest rates or credit spreads of securitization bonds,

1 the results presented in my testimony, including the proposed storm recovery
2 charges, should closely approximate the final figures.

3 My testimony addresses the following subject areas:

- 4 • The calculation of the proposed storm recovery charges for each
5 Company by customer rate class; and
- 6 • The tariff revisions needed to implement the storm recovery charges at
7 each Company.

8 **Q. ARE YOU SPONSORING ANY EXHIBITS TO YOUR DIRECT**
9 **TESTIMONY?**

10 A. Yes. The following exhibits are presented in conjunction with my Direct
11 Testimony:

- 12 • Byrd Exhibit 1 – Proposed Storm Recovery Costs by customer rate
13 class; and
- 14 • Byrd Exhibit 2 – Proposed Tariff Sheets by Company.

15 Each of these exhibits were prepared under my direction and control, and
16 to the best of my knowledge all factual matters contained therein are true and
17 accurate.

18 **II. CALCULATION OF THE STORM RECOVERY CHARGE**

19 **Q. PLEASE DISCUSS THE CALCULATION OF EACH STORM**
20 **RECOVERY CHARGE BY CUSTOMER RATE CLASS.**

21 A. The allocation methodology described in witness Abernathy's testimony is used
22 in the calculation of the storm recovery charge by customer rate class for each
23 Company in Abernathy Exhibit 3. The allocation factors used to calculate the

1 storm recovery charge were filed in DEC and DEP's most recent general rate
2 case dockets and were applied to the total first year revenue requirements
3 presented in Abernathy Exhibit 4 to allocate the revenue requirements to each
4 customer rate class. Next, the rate was calculated by dividing total revenue
5 requirements for each customer rate class by the effective kWh sales for each
6 customer rate class.

7 **Q. WILL EACH RATE CLASS'S STORM RECOVERY CHARGES**
8 **REMAIN FIXED OVER TIME?**

9 A. No. Each rate class's storm recovery charge will be subject to periodic
10 adjustments.

11 **Q. HOW WILL THE PERIODIC ADJUSTMENTS TO THE STORM**
12 **RECOVERY CHARGE BE DETERMINED?**

13 A. A formula-based true-up process will be used to make periodic adjustments to
14 the storm recovery charges. As described in witness Shana W. Angers' and
15 witness Charles N. Atkins II's testimonies, in any given period, differences
16 between the estimated and actual amount of storm recovery charge collections
17 and on-going financing costs will result in an adjustment to the storm recovery
18 charges.

19 **Q. PLEASE DESCRIBE HOW THIS FORMULA-BASED TRUE-UP WILL**
20 **WORK.**

21 A. At least semi-annually (or quarterly beginning 12 months prior to the scheduled
22 final payment date of the latest maturing tranche of each series of storm
23 recovery bonds) a new estimated revenue requirement for each Company's

1 storm recovery bonds will be calculated using the Storm Recovery Charge
2 True-Up Mechanism Form that witness Angers presents in Angers Exhibit 1.
3 This new estimated revenue requirement will take into account total financing
4 costs (including debt service) for the forecasted upcoming two periods and prior
5 period adjustments. Each Company will then calculate the customer rate impact
6 by customer rate class consistent with Byrd Exhibit 1, using the most current
7 Commission-approved allocation methodology and MWh sales forecast by rate
8 class from each Company's most recent Integrated Resource Plan for the period
9 over which the storm recovery charges will be billed. In addition to a semi-
10 annual true-up adjustment, each Company, acting as servicer for its series of
11 storm recovery bonds, will be permitted to file for optional interim true-up
12 adjustments at any time to ensure the recovery of revenues sufficient to provide
13 for the timely payment of the storm recovery bonds and all on-going financing
14 costs payable in connection with the storm recovery bonds.

15 **Q. WOULD THE SAME FORMULA-BASED MECHANISM BE USED IN**
16 **THE EVENT OF AN OVER-RECOVERY OF STORM RECOVERY**
17 **CHARGES TO ENSURE THE RECOVERY OF REVENUES MATCHES**
18 **THE TIMELY PAYMENT OF DEBT SERVICE FOR A SERIES OF**
19 **STORM RECOVERY BONDS AND ON-GOING FINANCING COSTS?**

20 A. Yes.

1 **Q. WHAT IS THE EXPECTED TREND IN THE STORM RECOVERY**
 2 **CHARGES OVER TIME?**

3 A. While it is impossible to know with certainty the trend in charges in advance,
 4 the storm recovery bonds have been structured to produce substantially stable
 5 annual charges over time. Assuming stable charges, the storm recovery charges
 6 are expected to vary inversely with expected load growth. In other words, each
 7 rate class's storm recovery charge should be relatively constant or slightly
 8 declining over time, barring unexpected load and cost variations.

9 **III. TARIFF SHEETS**

10 **Q. HAVE YOU DEVELOPED THE PROPOSED TARIFF SHEETS FOR**
 11 **EACH COMPANY NEEDED TO IMPLEMENT THE STORM**
 12 **RECOVERY CHARGES?**

13 A. Yes. Proposed tariff sheet numbers 133 and RR-35, which are provided in Byrd
 14 Exhibit 2, have been developed to implement the storm recovery charge for
 15 each Company.

16 **Q. DOES THE PROPOSED TARIFF LANGUAGE INDICATE THAT**
 17 **EACH STORM RECOVERY CHARGE IS A NONBYPASSABLE**
 18 **CHARGE?**

19 A. Yes. The following language is included to indicate the nonbypassable nature
 20 of the charge:

21 The Storm Recovery Charge shall be paid by all existing
 22 or future retail customers receiving transmission or
 23 distribution service, or both, from the Company or its

1 successors or assignees under Commission-approved
2 rate schedules or under special contracts, even if the
3 customer elects to purchase electricity from alternative
4 electric suppliers following a fundamental change in
5 regulation of public utilities in this State.

6 **Q. ARE THERE ANY TARIFF PROVISIONS SPECIFIC TO THE STORM**
7 **RECOVERY CHARGE?**

8 A. Yes. The following language is included on tariff sheets 133 and RR-35
9 indicating the ownership of the charge:

10 As approved by the Commission, a Special Purpose
11 Entity (“SPE”), wholly-owned by the Company, has
12 been created and is the owner of the storm recovery
13 property which includes all rights to impose, bill, charge,
14 collect, and receive the relevant Storm Recovery Charge
15 and to obtain periodic adjustment to such charges.
16 Company, as servicer, shall act as its SPE’s collection
17 agent for the relevant Storm Recovery Charge.

18 **Q. WHAT EFFECTIVE DATE ARE THE COMPANIES REQUESTING**
19 **FOR THE STORM RECOVERY CHARGE?**

20 A. DEC and DEP propose to implement the storm recovery charge related to their
21 series of storm recovery bonds beginning with the first billing cycle for the
22 month following the issuance of the storm recovery bonds. As explained in
23 witness Thomas J. Heath Jr.’s testimony, the Companies recommend an

1 issuance date as soon as practicable. Each storm recovery charge will remain
2 in effect until the related storm recovery bonds have been paid in full or legally
3 discharged and the financing costs associated with such series of storm recovery
4 bonds have been paid in full or fully recovered.

5 **Q. HOW WILL THE STORM RECOVERY CHARGES APPROVED BY**
6 **THE COMMISSION BE REFLECTED ON CUSTOMER BILLS?**

7 A. The storm recovery charges will be reflected by each Company as a separate
8 line on each customer's bill, titled "Storm Securitization Charge." This line
9 will include both the rate and the total amount charged. In addition, all electric
10 bills will state that, as approved in the Financing Orders, all rights to the Storm
11 Securitization Charge are owned by the relevant SPE and that DEC and DEP
12 are acting as a collection agent or servicer for such SPE.

13 **Q. ARE THE COMPANIES REQUESTING APPROVAL OF THE TARIFF**
14 **SHEETS ATTACHED IN BYRD EXHIBIT 2?**

15 A. Not at this time. As I mentioned previously, the final storm recovery charge for
16 each series of storm recovery bonds will not be calculated until after the final
17 terms of an issuance of such storm recovery bonds have been established. Once
18 the final storm recovery charge is calculated, the relevant tariff sheets shown in
19 Byrd Exhibit 2 will be revised and submitted for administrative approval by
20 noon on the 3rd business day after the date of submission of the tariff sheets as
21 part of the issuance advice letter process described in the testimony of witness
22 Heath. DEC and DEP are, however, requesting approval of the form of each
23 tariff sheet that is attached as Byrd Exhibit 2.

1 **Q. THEREAFTER, WOULD THE STORM RECOVERY CHARGE**
2 **TARIFF SHEETS BE REVISED PERIODICALLY?**

3 A. Yes. The formula-based true-up mechanism described earlier in my testimony
4 would result in revisions to the storm recovery charges listed on tariff sheet
5 numbers 133 and RR-35. DEC and DEP would seek administrative approval
6 of any necessary revisions to these tariff sheets resulting from the formula-
7 based true-up mechanism as part of the overall administrative approval of the
8 true-up adjustment.

9 **IV. CONCLUSION**

10 **Q. PLEASE SUMMARIZE YOUR TESTIMONY.**

11 A. I have provided support for the calculation of the storm recovery charges and
12 their components by rate class. Lastly, I have outlined the tariff revisions
13 needed to implement the storm recovery charges.

14 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

15 A. Yes

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION**DOCKET NO. E-7, SUB 1243****DOCKET NO. E-2, SUB 1262**

In the Matter of:)	
	)	DIRECT TESTIMONY OF
Petition of Duke Energy Carolinas, LLC	)	SHANA W. ANGERS
And Duke Energy Progress, LLC for	)	FOR DUKE ENERGY
Issuance of Storm Cost Recovery Financing)	CAROLINAS, LLC AND DUKE
Orders)	ENERGY PROGRESS, LLC

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I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Shana W. Angers, and my business address is 550 South Tryon Street, Charlotte, North Carolina.

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

A. I am employed by Duke Energy Business Services, LLC as Accounting Manager for Duke Energy Progress, LLC (“DEP”), testifying on behalf of DEP and Duke Energy Carolinas, LLC (“DEC”) (each a “Company” or collectively “the Companies”).

Q. PLEASE BRIEFLY SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL EXPERIENCE.

A. I graduated from the University of Florida with a Bachelor of Science degree and Master’s degree in Accounting. I am also a Certified Public Accountant licensed in the state of Florida and maintain a reciprocal license in the state of North Carolina. I have 12 years of professional experience with Duke Energy Corporation (“Duke Energy”) in various accounting and finance roles. I was named to my current position as Accounting Manager of DEP in December 2018.

Q. WHAT ARE YOUR RESPONSIBILITIES IN YOUR CURRENT POSITION?

A. I am responsible for ensuring that the accounting impacts of DEP’s business activities and transactions are understood and properly recorded to the general ledger and that such accounting impacts, as well as any applicable related

1 variances to budget and prior year results, are clearly explained and properly
2 presented in internal and/or external financial reports. I am also responsible for
3 ensuring that the accounting team performs its tasks in an accurate and timely
4 manner in accordance with published deadlines while strictly adhering to
5 Company policies and controls.

6 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE NORTH**
7 **CAROLINA UTILITIES COMMISSION (“COMMISSION”)?**

8 A. Yes. I most recently testified before this Commission in DEP’s most recent
9 general rate case proceeding in Docket No. E-2, Sub 1219.

10 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**
11 **PROCEEDING?**

12 A. The purpose of my testimony is to (i) propose the mechanism and
13 corresponding form to be used for making periodic, formula-based true-ups to
14 the proposed charges to customers to pay the Companies’ storm recovery costs
15 and financing costs as a result of Hurricanes Florence, Michael, Dorian, and
16 Winter Storm Diego, the “storm recovery charges” and (ii) present the
17 accounting entries that will be required for the proposed storm recovery charges
18 for each Company.

19 **Q. WILL THERE BE MULTIPLE STORM RECOVERY CHARGES?**

20 A. There will be a single storm recovery charge dedicated for each series of storm
21 recovery bonds issued on behalf of either DEC or DEP. Each storm recovery
22 charge will be paid by all existing or future retail customers receiving

1 transmission or distribution services, or both, from either DEP or DEC, as the
2 case may be, or their successors or assignees.

3 **Q. ARE YOU SPONSORING ANY EXHIBITS WITH YOUR DIRECT**
4 **TESTIMONY?**

5 A. Yes. The following exhibits are presented in conjunction with my direct
6 testimony:

- 7 • Angers Exhibit 1 – Storm Recovery Charge True-Up Mechanism Form
- 8 • Angers Exhibit 2 – Accounting Entries to Record Storm Recovery
- 9 Charge

10 Each of these exhibits were prepared under my direction and control, and to
11 the best of my knowledge all factual matters contained therein are true and
12 accurate.

13 **II. TRUE-UP MECHANISM**

14 **Q. DO THE COMPANIES HAVE A STATUTORY OBLIGATION TO**
15 **PERIODICALLY TRUE-UP THEIR STORM RECOVERY CHARGES?**

16 A. Yes. Per Section (b)(3)b.6. of N.C. Gen. Stat. § 62-172 (the “Securitization
17 Statute”):

18 “A financing order issued by the Commission to a public utility shall include...

- 19 6. A formula-based true-up mechanism for making, at least annually,
- 20 expeditious periodic adjustments in the storm recovery charges that
- 21 customers are required to pay pursuant to the financing order and for
- 22 making any adjustments that are necessary to correct for any overcollection
- 23 or under collection of the charges or to otherwise ensure the timely payment

1 of storm recovery bonds and financing costs and other required amounts
2 and charges payable in connection with the storm recovery bonds.”

3 **Q. HOW WILL THE TRUE-UP MECHANISM WORK?**

4 A. Per Section (b)(3)d. of the Securitization Statute, the Companies are required to
5 file with the Commission, at least annually, a petition or letter applying the
6 formula-based true-up mechanisms and, based on estimates of consumption for
7 each rate class and other mathematical factors, request approval to make the
8 applicable adjustments. Within 30 days after receiving the Companies’ filing,
9 the Commission is required to either approve the request or inform the
10 Companies of any mathematical or clerical errors in its calculation.

11 To achieve this, at least semi-annually (or quarterly beginning 12
12 months prior to the scheduled final payment date of the latest maturing tranche
13 of each series of storm recovery bonds) a new estimated revenue requirement
14 for each Company’s storm recovery bonds will be calculated using the Storm
15 Recovery Charge True-Up Mechanism Form presented in Angers Exhibit 1.
16 This new estimated revenue requirement will take into account total financing
17 costs (including debt service) for the forecasted upcoming two periods and prior
18 period adjustments. Once the total average retail storm recovery charge per
19 kWh is calculated for a specific series of storm recovery bonds for the upcoming
20 remittance period, it is broken down to specific charges per customer rate class.
21 This breakdown is further addressed in witness Melissa Abernathy’s testimony.

1 **Q. HOW OFTEN DO THE COMPANIES INTEND TO TRUE-UP THE**
2 **STORM RECOVERY CHARGES?**

3 A. The Companies propose to implement a true-up at least semi-annually. The
4 Companies propose to make their semi-annual true-up filings so that each semi-
5 annual true-up shall be effective approximately three months prior to the next
6 scheduled payment date. This true-up mechanism will help to ensure that
7 customers pay no more or less than what is required to pay the debt service on
8 the storm recovery bonds and all on-going financing costs. The calculation will
9 take into account total financing costs (including debt service) for the forecasted
10 upcoming two periods and prior period adjustments. It will also help mitigate
11 bondholders' exposure to differences in actual and estimated sales forecasts,
12 uncollectable accounts receivable, and cash flow variability.

13 **Q. PLEASE DESCRIBE THE TIMELINE FOR EACH SEMI-ANNUAL**
14 **TRUE-UP FILING.**

15 A. Assuming the storm recovery bonds are issued on June 1, 2021, as proposed by
16 DEC and DEP, the storm recovery bonds will have scheduled payment dates of
17 January 1 and July 1. To ensure storm recovery charge collections are sufficient
18 to ensure timely payment of the storm recovery bonds and all on-going
19 financing costs, the Companies propose making the semi-annual true-up filings
20 at the end of February and August so that each true-up adjustment of storm
21 recovery charges will be effective on April 1 and October 1 of each year.

1 **Q. WILL OVER OR UNDER RECOVERIES OF THE STORM**
2 **RECOVERY CHARGES BE TRACKED ON A CLASS-BY-CLASS**
3 **BASIS FOR DETERMINING FUTURE CHARGES?**

4 A. No. Any over or under recoveries for any prior period will simply be used to
5 adjust the periodic revenue requirement for the next period, thus benefiting all
6 customers classes. This “cross collateralization” will strengthen the security
7 for the storm recovery bonds.

8 **Q. WILL STORM RECOVERY CHARGES BE “CROSS**
9 **COLLATERALIZED” FOR ALL SERIES OF STORM RECOVERY**
10 **BONDS?**

11 A. No. As noted above, each series of storm recovery bonds will have its own
12 dedicated storm recovery charge. Retail customers will only be obligated to
13 pay amounts due with respect to the dedicated storm recovery charges
14 applicable to them. As a result, retail customers of DEC will have no obligation
15 to pay storm recovery charges related to storm recovery bonds issued to recover
16 storm recovery costs of DEP and retail customers of DEP will have no
17 obligation to pay storm recovery charges related to storm recovery bonds issued
18 to recover storm recovery costs of DEC.

19 **Q. APART FROM THE SEMI-ANNUAL TRUE-UP ADJUSTMENTS, DO**
20 **THE COMPANIES SEEK AUTHORITY TO FILE A TRUE-UP AT ANY**
21 **OTHER TIME?**

22 A. Yes. In addition to the semi-annual true-up adjustments, each Company, acting
23 as servicer for its series of storm recovery bonds, seeks authority to make

1 optional, interim true-up adjustments at any time to ensure the recovery of
2 revenues sufficient to provide for the timely payment of the storm recovery
3 bonds and all on-going financing costs payable in connection with the storm
4 recovery bonds. The optional true-up adjustment would follow the same
5 process and use the same form, contained in Angers Exhibit 1, as the
6 semiannual true-up adjustment. The approval period for the optional, interim
7 true-up adjustment would also be within 30 days of the date of filing.

8 **Q. HOW LONG WILL THE STORM RECOVERY CHARGES BE**
9 **IMPOSED AND COLLECTED?**

10 A. Each storm recovery charge will be imposed and collected until its series of
11 storm recovery bonds have been paid in full or legally discharged and the
12 related financing costs have been paid in full or fully recovered.

13 **Q. WILL THE COMPANIES RECONCILE STORM RECOVERY**
14 **CHARGE COLLECTIONS AND ESTIMATED REMITTANCES?**

15 A. Yes. At least semi-annually, each Company will reconcile storm recovery
16 charge collections during the prior six months with amounts remitted. If storm
17 recovery charges have been under-remitted, each Company will remit the
18 shortfall to the indenture trustee on the next servicer business day. If the storm
19 recovery charges have been over-remitted, then the relevant Company will
20 reduce the next succeeding remittance(s) by the amount of the over-remittance.
21 Each Company will also update the data underlying the weighted average days
22 outstanding and delinquency factors.

1 **Q. WHAT WILL HAPPEN WITH STORM RECOVERY CHARGE**
2 **COLLECTIONS FOLLOWING REPAYMENT OF THE STORM**
3 **RECOVERY BONDS AND ANY RELATED FINANCING COSTS?**

4 A. After all storm recovery bonds and on-going financing costs of a particular
5 series have been paid in full, the relevant storm recovery charge will no longer
6 be billed to, or collected from, customers. Any remaining amounts held by the
7 relevant special purpose entity (“SPE”) (exclusive of the amounts in the capital
8 subaccount, representing the equity contribution, together with any return on
9 the capital subaccount) will be remitted to DEC or DEP, as applicable, to be
10 credited to customers’ bills.

11 **III. ACCOUNTING FOR STORM RECOVERY**

12 **Q. PLEASE DESCRIBE THE OVERALL ACCOUNTING TREATMENT**
13 **FOR STORM RECOVERY FINANCING.**

14 A. As explained in witness Charles N. Atkins II’s direct testimony, the Companies
15 will conduct storm recovery financing through SPEs. Each SPE will be created
16 solely to facilitate storm recovery cost financing and will be a wholly-owned
17 subsidiary of either DEC or DEP. The SPEs and the Companies will maintain
18 separate accounting records. The accounting entries necessary to record storm
19 recovery financing activities (e.g., initial bond issuance, monthly collections,
20 etc.), along with an explanation of each, are illustrated in my Exhibit 2.

1 **Q. ARE THE COMPANIES REQUESTING COMMISSION APPROVAL**
2 **FOR ANY SPECIFIC ACCOUNTING TREATMENT ASSOCIATED**
3 **WITH THE PROPOSED STORM RECOVERY COST FINANCINGS?**

4 A. Yes. Each Company is seeking approval to sell the right to impose, bill, charge,
5 collect and receive the storm recovery charges authorized under a financing
6 order, and to obtain periodic adjustments to such charges, to its SPE and to
7 classify such right as storm recovery property as defined in the Securitization
8 Statute.

9 **Q. WHAT AMOUNTS OF STORM RECOVERY PROPERTY ARE THE**
10 **COMPANIES PROPOSING TO SELL TO THEIR SPEs?**

11 A. DEC is proposing to sell storm recovery property in the approximate amount of
12 \$230.8 million to its SPE which, assuming a June 1, 2021 issuance, includes
13 approximately \$37.2 million of carrying costs and DEP is proposing to sell
14 storm recovery property in the approximate amount of \$748.0 million to its SPE
15 which, assuming a June 1, 2021 issuance, includes approximately \$113.8
16 million of carrying costs. Additionally, all paid (or accrued) upfront financing
17 costs, primarily bond issuance costs, will also be included in the amounts
18 funded through the bond financings at the SPEs.

19 **Q. HOW WILL THE SPEs AMORTIZE STORM RECOVERY**
20 **PROPERTY?**

21 A. Each SPE will amortize the relevant storm recovery property based on the
22 principal amount required for the repayment of the relevant series of storm
23 recovery bonds over the expected life of the bonds.

1 **Q. WHAT ARE THE ANTICIPATED ACCOUNTING ENTRIES TO BE**
2 **RECORDED AT THE SPE?**

3 A. As illustrated in my Exhibit 2, the accounting entries to be recorded by the SPEs
4 are as follows: (1) recording of capital subaccount from the Companies' equity
5 investment; (2) recording of proceeds from the issuance of bonds; (3) purchase
6 of storm recovery property from each Company; (4) receipt of cash from the
7 relevant Company for the storm recovery charges collected; (5) amortization of
8 the storm recovery property; (6) accrual of interest expense; (7) amortization of
9 up-front financing costs; (8) payment of bond principal and interest; (9)
10 recording of on-going operating costs and servicing fees payable; (10)
11 replenishment of capital subaccount, if needed; (11) return impacts on the
12 capital subaccount; and (12) transfer of cash to the excess funds subaccount in
13 the event of excess storm recovery charges collected.

14 **Q. WHAT ARE THE ANTICIPATED ACCOUNTING ENTRIES TO BE**
15 **RECORDED AT THE COMPANIES?**

16 A. As illustrated in Angers Exhibit 2, the accounting entries to be recorded by each
17 Company are as follows: (1) recording of expenditure of cash to fund the
18 capital subaccount at each SPE and a related investment; (2) sale of the storm
19 recovery property to each SPE; (3) recognition and collection of storm recovery
20 charges; (4) collection and remittance of revenue related taxes on the storm
21 recovery charges (*i.e.*, gross receipts tax, franchise fee, etc.); (5) interest on
22 remittances (only if applicable); and (6) impact of earnings of each SPE.

1 **Q. HOW WILL STORM RECOVERY CHARGES COLLECTED FROM**
2 **CUSTOMERS BE RECORDED?**

3 A. The storm recovery charge collections will be remitted to and recorded as
4 revenues at the relevant SPE.

5 **Q. PLEASE DESCRIBE HOW EACH COMPANY, AS SERVICER,**
6 **PROPOSES TO REMIT STORM RECOVERY CHARGES TO THE**
7 **SPE.**

8 A. Each Company, as servicer, will be required to remit storm recovery charges
9 directly to the appropriate Bond Trustee for each series of storm recovery
10 bonds. As the Companies do not track its customer charges on a daily basis,
11 they will remit storm recovery charges based on estimated daily collections
12 using a weighted average balance of days outstanding (“ADO”) on the
13 Companies’ retail bills. Collections remitted daily will represent the charges
14 estimated to have been received on any day, based upon the ADO and estimated
15 write-offs. For example, if a Company’s retail bills are outstanding, on a
16 weighted average basis, for a period of thirty days, then such Company will
17 remit to the appropriate SPE the storm recovery charges estimated to be
18 collected on a particular date, less an assumed delinquency rate, thirty days
19 thereafter.

20 **Q. CAN THE COMPANIES REMIT THE STORM RECOVERY**
21 **CHARGES LESS FREQUENTLY THAN DAILY UNDER CERTAIN**
22 **CONDITIONS?**

23 A. Yes, under certain circumstances. Provisions within the servicing agreement

1 may also permit each Company to remit storm recovery charges monthly,
2 instead of daily. The Company may only exercise this option if the conditions
3 of the servicing agreement are satisfied. These conditions will be driven by
4 rating agency requirements to achieve and maintain the targeted “AAA” ratings
5 on the bonds and may include the maintenance by the Companies of a minimum
6 credit rating(s), the maintenance of reserves, or other conditions. If the
7 Companies are eligible to remit charges monthly, and elect to do so, then
8 charges would be remitted based upon the same general methodology. For
9 example, assuming again that charges are outstanding on average for thirty
10 days, then all charges which are assumed to be collected during a calendar
11 month will be remitted on the first business day of the next calendar month.
12 The Companies would include in any remittance investment earnings which are
13 estimated to have been earned on such collections in the hands of the
14 Companies. A monthly remittance process for the storm recovery charges
15 would only occur if it does not negatively impact the credit ratings for the
16 bonds.

17 **Q. HOW WILL THE COMPANIES ALLOCATE PARTIAL PAYMENTS**
18 **ON A BILL TO THE STORM RECOVERY CHARGES?**

19 A. When each Company, acting as servicer, does the annual reconciliation, partial
20 payments will be allocated to the appropriate storm recovery charges in the
21 same proportion that such charges bear to the total bill. The first dollars
22 collected would be attributed to past due balances, if any. Once those balances
23 are paid in full, if cash collections are not sufficient to pay a customer’s current

1 bill, then the cash would be prorated between the different components of the
2 bill.

3 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

4 **A. Yes.**

1 CHAIR MITCHELL: And, Mr. Robinson, we
2 do have a request for you for a late-filed exhibit
3 related to the Angers testimony. Would the
4 Companies provide as a late-filed exhibit a revised
5 Angers Exhibit 2, page 1 of 1, which is an exhibit
6 of the direct testimony which reflects the matters
7 agreed upon in the agreement and stipulation of
8 partial settlement.

9 MR. ROBINSON: Yes, Chair Mitchell,
10 understood.

11 CHAIR MITCHELL: Okay.

12 All right. With that, we will turn to
13 Public Staff. Mr. Grantmyre, call a witness.

14 MR. GRANTMYRE: Yes. The Public Staff
15 would call the panel of Mr. Sutherland and
16 Mr. Heller.

17 CHAIR MITCHELL: All right.
18 Mr. Sutherland and Mr. Heller, let me identify you
19 on my screen. Let's see here. There you are,
20 Mr. Sutherland. There are you, Mr. Heller.

21 Whereupon,

22 PAUL R. SUTHERLAND AND STEVEN HELLER,
23 having first been duly affirmed, were examined
24 and testified as follows:

1 CHAIR MITCHELL: All right.

2 Mr. Grantmyre, you may proceed.

3 MR. GRANTMYRE: Just for advice,
4 William Grantmyre will sponsor Mr. Sutherland, and
5 Mr. Creech will sponsor Mr. Heller, and we will
6 start with Mr. Sutherland.

7 DIRECT EXAMINATION BY MR. GRANTMYRE:

8 Q. Mr. Sutherland, will you please state your
9 name and address?

10 A. (Paul R. Sutherland) My name is
11 Paul R. Sutherland. My work address is Saber Partners
12 at 260 Madison Avenue, Suite 8019, New York, New York
13 10016.

14 Q. And you are testifying in this case on behalf
15 of the Public Staff?

16 A. Yes, I am.

17 Q. Now, did you cause to be prefiled in this
18 case direct testimony consisting of 43 pages and 10
19 [sic] exhibits?

20 A. Yes, I did.

21 Q. Now, if I were to ask you those same
22 questions again today, would your answers be the same?

23 A. Yes, they would.

24 MR. GRANTMYRE: Madam Chair, I request

1 that his direct testimony be copied into the record
2 as if given orally and that his exhibits be
3 identified.

4 CHAIR MITCHELL: All right. The direct
5 testimony of the witness prefiled on
6 December 21, 2020, in these dockets shall be --
7 consisting of 43 pages, shall be copied into the
8 record as if delivered orally from the stand. And
9 the exhibits to that testimony shall be identified
10 as they were when prefiled.

11 (Sutherland Exhibits 1 through 11, were
12 identified as they were marked when
13 prefiled.)

14 (Reporter's Note: See dialogue below
15 regarding corrected testimony.)

16 Q. Now, also, on January 26, 2021, did you file
17 errata corrective testimony, and if I were to ask you
18 the same questions today as to the corrective part,
19 would your answer be the same?

20 A. Yes, it would.

21 MR. CREECH: I believe that's
22 January 6th.

23 MR. GRANTMYRE: Okay. January 6th.
24 Madam Chair, I would ask that that testimony be

1 copied into the record as if given orally.

2 CHAIR MITCHELL: All right. Hearing no
3 objection, Mr. Grantmyre, the errata testimony of
4 the witness that was filed with this Commission on
5 January 6, 2021, shall be copied into the record as
6 if given orally from the stand.

7 (Whereupon, the prefilled corrected
8 direct testimony of Paul R. Sutherland
9 was copied into the record as if given
10 orally from the stand.)
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BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

Docket No. E-2, Sub 1262

Docket No. E-7, Sub 1243

In the Matter of
Joint Petition of Duke Energy)
Carolinas, LLC and Duke Energy)
Progress, LLC Issuance of Storm)
Recovery Financing Orders)

Direct Testimony of
PAUL SUTHERLAND, SENIOR
ADVISOR – Saber Partners,
LLC

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

**Docket No. E-2, Sub 1262
Docket No. E-7, Sub 1243**

**Direct Testimony of
Paul Sutherland, Senior Advisor
Saber Partners, LLC
December 21, 2020**

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TESTIMONY OF PAUL R. SUTHERLAND
DECEMBER 21, 2020

Introduction

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. Paul R. Sutherland, Saber Partners, LLC (Saber or Saber
3 Partners), 260 Madison Avenue, Suite 8019, New York, New York
4 10016.

5 **Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR**
6 **POSITION?**

7 A. I am with Saber Partners, LLC, and serve as a Senior Advisor.

8 **Q. PLEASE DESCRIBE YOUR DUTIES AND RESPONSIBILITIES**
9 **IN THAT POSITION.**

10 A. My responsibilities with Saber include work in data management,
11 financial modeling, financial analysis, issuance cost auditing, deal
12 structuring, pricing analysis with respect to relative value and
13 review of issuance advice letters, mostly on behalf of public utility
14 commission clients and generally related to utility sponsored
15 Ratepayer-Backed-Bond (RBB) financing. I have performed these
16 functions while advising the following regulatory bodies regarding
17 utility securitizations: Public Utility Commission of Texas, West
18 Virginia Public Service Commission, New Jersey Board of Public
19 Utilities, Florida Public Service Commission, and the Wisconsin

1 Public Service Commission. I have also provided testimony on
2 behalf of the California Community Choice Association.

3 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND**
4 **AND PROFESSIONAL EXPERIENCE.**

5 A. I have a bachelor's degree in electrical engineering from Cornell
6 University. I also have a master's degree in business
7 administration from the University of Chicago.

8 I began working with Florida Power & Light Company (FPL) in
9 1976 doing economic analysis of new energy technologies in the
10 Research and Development (R&D) Department. After several
11 years, I moved to the Finance Department as a Financial Analyst.
12 Over the next 20 years I held various positions, including
13 Coordinator of Financial Systems, Manager of Corporate Finance,
14 Manager of Financial Analysis and Forecasting, and Assistant
15 Treasurer of both the utility and FPL Group Capital. Before leaving
16 FPL in 1998, I was Director of Finance, Accounting & Systems for
17 the FPL Energy Marketing and Trading Division. During my time
18 with FPL, I testified as an expert witness on cost of capital and
19 financial integrity. I also taught classes on economic decision-
20 making and on quality improvement. It was during this time (1989)
21 that FPL became the first non-Japanese company to win the
22 Deming Prize for Total Quality Management.

1 In 2000, after a year as adjunct professor of mathematics at Palm
2 Beach Atlantic College, I joined Saber Partners, LLC, as a Senior
3 Managing Director. I have been associated with Saber Partners
4 since that time in various roles, including my current position as
5 Senior Advisor. I have taken part in 13 investor-owned utility
6 securitization financings that raised over \$9 billion in capital for
7 eight different utilities.

8 **Q. PLEASE PROVIDE SOME OF YOUR BACKGROUND AND**
9 **EXPERIENCE WITH UTILITY FINANCINGS WHILE YOU WERE**
10 **AT FPL.**

11 A. While at FPL, as Manager of Corporate Finance and Assistant
12 Treasurer, I helped FPL complete over \$2 billion of debt and equity
13 financings in the public capital markets. FPL executed both
14 competitive and negotiated securities offering transactions. FPL
15 was also among the first to issue long-term variable rate tax-
16 exempt debt that could be (and was) later converted to a fixed
17 rate. Part of my job, along with the Treasurer and Chief Financial
18 Officer, was to prepare and deliver rating agency presentations to
19 support the credit ratings from the three major rating agencies.

20 **List of Exhibits**

21 **Q. ARE YOU SPONSORING ANY EXHIBITS IN THIS CASE?**

22 A. Yes, I am sponsoring:

1

2 Exhibit 1, List of Prior Utility Securitization Transactions with
3 Tranches and Weighted Average Lives (WALs)

4 Exhibit 2, 2001-2006 Texas vs Non-Texas Deals

5 Exhibit 3, Citigroup Analysis of Texas Interest Savings

6 Exhibit 4, 2001 to 2012 – Spreads to Swaps of 9-10 Year WAL
7 Tranches

8 Exhibit 5, Methodology for Relative Value Benchmarking

9 Exhibit 6, Standard Deviation of Spreads to Swaps vs. Spreads to
10 Agencies

11 Exhibit 7, Duke Energy Florida (DEF) Interest Savings

12 Exhibit 8, Atkins' Interest Rate Assumptions

13 Exhibit 9, How Much Does Size Matter?

14 Exhibit 10, AYE (Alleghany Energy Inc.) 2009 Interest Savings

15 Exhibit 11, Glossary

16 **Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS**
17 **PROCEEDING?**

18 A. I am testifying on behalf of the Public Staff of the North Carolina
19 Utilities Commission, which represents the interests of the
20 ratepayers of Duke Energy Carolinas, LLC (DEC), and Duke

1 Energy Progress, LLC (DEP) (together, "the Companies"), relating
2 to the utilities' proposed use of storm recovery bond (SRB)
3 financing. The Public Staff hired Saber Partners, LLC, as its
4 consultant in this proceeding.

5 **Purpose of Testimony**

6 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

7 A. The purpose of my testimony is to

- 8 • discuss and demonstrate how ratepayers benefit from RBB
9 financing, and more specifically, ways in which that benefit can be
10 measured and maximized through optimal structuring and
11 application of "best practices" by a Bond Team,
- 12 • explain how negotiated bond pricing can be evaluated under
13 market conditions leading up to, and at the time of pricing based
14 upon relative value with respect to comparable benchmark
15 securities,
- 16 • discuss reasons for and potential benefits of extending final
17 maturity beyond 15 years,
- 18 • point out several misleading or erroneous statements,
19 calculations, or assumptions in the testimony of the Companies'
20 witness Atkins, some of which carry over into the exhibits of the
21 Companies' witness Abernathy.

- 1 • suggest certain other changes to the proposed Financing Order.

2 Since some of the terms that I and other witnesses use may be
3 unfamiliar to those who have not previously been involved in this
4 type of utility securitization financing, I have included a glossary of
5 terms as Exhibit 11.

6 **Q. DO YOU KEEP TRACK OF ALL UTILITY SECURITIZATION**
7 **TRANSACTIONS?**

8 A. I do. Exhibit 1 shows a list of 67 distinct utility securitization
9 transactions that have occurred since 1997. I maintain this list as
10 part of Saber's database of documents and statistics from each of
11 the 67 prior deals. The exhibit includes principal amount by
12 tranche (sometimes also called "series" in the context of corporate
13 bonds) and the weighted average life (WAL), in years, for each
14 tranche.

15 **Q. DOES YOUR LIST AGREE WITH DEF WITNESS ATKINS'**
16 **EXHIBIT 3?**

17 A. Not exactly. Our list includes the \$482.9 million taxable portion of
18 the Long Island Power Authority (LIPA) 2013 securitization
19 transaction. Neither of our lists includes the tax-exempt portion of
20 the offering, since those bonds were priced and sold in the
21 municipal market. Because the interest for bonds issued into that
22 market is exempt from federal income taxes, the market for those

1 LIPA bonds is different from the market for all other investor-
2 owned utility transactions, as the tax advantage gives those LIPA
3 bonds an advantage in pricing over bonds without federal tax-
4 exempt interest. None of the SRB debt in this proceeding will be
5 tax-exempt municipal securities that have such a different investor
6 base.

7 Another difference is that the Atkins list misstates the pricing date
8 of the Hawaiian Electric transaction as 11/13/14 when, in fact it,
9 was 11/4/2014.

10 **Determinants of Savings and Role of Bond Team**

11 **Q. WHERE DO RATEPAYER SAVINGS COME FROM IN A**
12 **UTILITY SECURITIZATION?**

13 A. The biggest net present value (NPV) savings result from
14 the fact that rating agencies generally treat utility securitization
15 debt as off-balance sheet. This means that, unlike conventional
16 utility debt, securitization debt does not need to be offset with a
17 similar amount of common equity to maintain an acceptable
18 capital structure. The avoidance of the high cost of equity, together
19 with the associated state and federal income taxes, can account
20 for as much as two thirds of the total savings. Most of the rest of
21 the NPV savings comes from the fact that securitization payments
22 are usually levelized, as will be the case with this SRB financing,

1 whereas traditional utility financing has a structure with declining
2 revenue requirements. A relatively smaller contribution to savings
3 comes from the interest rate differential between AAA-rated
4 securitization debt and traditional, lower rated utility debt. To some
5 degree, these savings are going to be present, regardless of how
6 well the financing is executed.

7 **Q. WHAT ARE THE BIGGEST DETERMINANTS OF RATEPAYER**
8 **SAVINGS OVER WHICH THE BOND ISSUER HAS SOME**
9 **CONTROL IN AN SRB FINANCING?**

10 A. There are two major determinants in addition to various smaller
11 factors that affect ratepayer savings. The first is the interest rate
12 that the ratepayer has to pay on the bonds. The second is the
13 structure of the financing, which can include the time period over
14 which the ratepayer has to repay the principal amount that is being
15 financed or the size or number of the tranches (or series) that
16 make up the total financing, or even the legal framework used. In
17 each case, the final determination of each of the two factors is
18 limited by constraints that may or may not be beyond the control
19 of the issuer. In most cases the issuer has some control over both
20 the interest rate and the structure. Also, when I refer to the issuer
21 in this context, I am really talking about the entire Bond Team,
22 defined as a team comprised of the sponsoring utility, the Utilities
23 Commission, the Public Staff, their financial advisors, and others

1 who are all, presumably, working on behalf of the ratepayers,
2 since unlike conventional utility debt, with SRBs the ratepayer is
3 directly responsible for repayment of the bonds. In my opinion, this
4 is the strongest reason why the Public Staff and its advisors should
5 have equal say with the utilities in planning and execution of the
6 financing in question. The admittedly limited control that the issuer
7 has over interest rates and structure can nonetheless have major
8 impacts on the NPV savings over the life of the bonds.

9 **Q. IN YOUR VIEW, SHOULD THE COMMISSION GIVE THE**
10 **COMPANIES BROAD FLEXIBILITY TO ESTABLISH THE**
11 **FINAL TERMS AND CONDITIONS OF THE BONDS AS**
12 **SUGGESTED BY ITS WITNESSES ATKINS AND HEATH?**

13 A. No. Were these normal utility bonds subject to standard review
14 and approval by the Commission, the Commission could easily
15 grant that broad flexibility because it would have the authority for
16 an unlimited after-the-fact review. In this case, however, the
17 Commission does not have that opportunity, as described by other
18 witnesses. As such, the Commission's Order in this proceeding
19 should require that the final terms and conditions be determined
20 in a joint, collaborative process with the Commission, the Public
21 Staff, and/or its independent advisors participating actively, visibly,
22 and in real-time. The exhibits I am sponsoring, I believe, amply
23 demonstrate the benefits that accrue to ratepayers from

1 employing best practices, and in particular, from providing the
2 Public Staff and its advisors equal authority with other members
3 of a Bond Team to make major decisions involving structuring,
4 marketing, and pricing of the SRBs.

How Interest Rates Are Established

5 **Q. PLEASE EXPLAIN HOW THE INTEREST RATE ON RBB**
6 **FINANCING IS DETERMINED UNDER ANY PARTICULAR SET**
7 **OF MARKET CONDITIONS.**

8 A. RBBs, in this case SRBs, are normally priced by establishing a
9 spread between the yield or bond interest rate and a particular
10 benchmark security. Historically, most such bonds have been
11 priced based on a spread known as an interest rate swap security,
12 similar to how asset-backed securities customarily are priced.
13 However, as Public Staff witness Heller explains, securitization
14 debt is not really an asset-backed security, although it may have
15 some characteristics in common. Consequently, in the case of the
16 Duke Energy Florida (DEF) storm recovery financing in 2016, the
17 bonds were priced relative to U.S. Treasury bonds, which is the
18 benchmark typically used for corporate debt securities. Either way,
19 the market determines the yields on the pricing benchmark
20 securities, either swaps or U.S. Treasury bonds. Then, the issuer
21 negotiates a spread based on one or the other of the benchmarks
22 and that determines the actual interest rate on the bonds. As an

1 example, in the case of the DEF nuclear asset recovery bond sale
2 in 2016, the five-year series, that is to say the series with a WAL
3 of five years, was priced from the five-year U.S. Treasury bond
4 with a coupon of 1.375% which was yielding 1.131% at the time.
5 The Bond Team negotiated a spread of 60 basis points or 0.60%,
6 so the yield on the nuclear asset recovery bond five-year series
7 was set at 1.731%. Since market prices and yields change minute
8 to minute, it is impossible to say exactly what the final yield will be
9 until the moment of pricing. However, the issuer and investors can
10 agree on the 60-basis point spread in the minutes or hours
11 beforehand to avoid worry about last minute movements in the
12 market.

13 **Q. WHAT HAPPENS IF THERE IS NO PRICING BENCHMARK**
14 **SECURITY WITH EXACTLY THE SAME MATURITY AS THE**
15 **WAL OF THE SERIES BEING PRICED?**

16 A. In that case, the issuer and investors will look for pricing
17 benchmarks with maturities that are near to the WAL of the
18 securitization series. In such situations, some underwriters like to
19 negotiate a spread to the pricing benchmark that has the closest
20 maturity to the RBB WAL. For example, consider the 15.2-year
21 WAL series in the DEF deal. Underwriters might prefer to price the
22 series off of the 10-year U.S. Treasury bond. That bond had a
23 coupon of 1.625%, was due on 5/15/26, and yielded 1.608%. The

1 spread to such a pricing benchmark is known as the T-spread and
2 was 125 basis points at the time of pricing. However, it is difficult
3 for the issuer to judge the reasonableness of such pricing due to
4 the difference between the WALs of the two securities (10 years
5 versus 15.2 years).

6 **Q. IS THERE A BETTER WAY TO PRICE SUCH BOND SERIES?**

7 A. A better way to price such series is to interpolate between the
8 closest pricing benchmark securities on either side of the WAL of
9 the series in question. Thus, in the case of the 15.2-year WAL
10 series, the issuer can interpolate between the 10-year U.S.
11 Treasury bond and the 30-year U.S. Treasury bond to get a rate
12 that corresponds to a theoretical 15.2-year Treasury rate. That
13 interpolated rate would be approximately 1.826%. The spread
14 between the interpolated U.S. Treasury bond rate and the rate on
15 the RBB being priced is known as the g-spread. In this case, the
16 g-spread was approximately 103 basis points, so the 15.2-year
17 series was priced a little more than 1.03% above the interpolated
18 U.S. Treasury bond rate of 1.826% to yield 2.858%. The g-spread,
19 although not generally favored by underwriters as a pricing
20 benchmark, is more often used by investors in deciding whether
21 or not to purchase bonds.

Power of the Issuer and Measuring Performance

1 **Q. HOW MUCH ABILITY DOES THE ISSUER HAVE TO**
2 **NEGOTIATE THE YIELD ON THE BONDS?**

3 A. While the issuer has no ability to negotiate the underlying pricing
4 benchmark rate, be it the swap rate or the U.S. Treasury bond
5 rate, the issuer can certainly negotiate the spread off of those
6 pricing benchmark rates. The presence or absence of certain best
7 practices as discussed by Public Staff witnesses Fichera,
8 Abramson, Maher, and Klein is a major factor in determining the
9 likely success of such negotiations. For example, the financial
10 advisor to the Commission or to the Public Staff most directly
11 represents the ratepayer and therefore has the greatest incentive
12 to negotiate the lowest interest rate consistent with market
13 conditions. If the advisor has the authority as a Bond Team
14 member to fully participate in the structuring, marketing, and
15 pricing of the bonds, there will be greater ability to negotiate the
16 tightest possible credit spreads and therefore the lowest possible
17 yields on the bonds.

18 **Q. WHAT EVIDENCE IS THERE THAT SUCH BEST PRACTICES**
19 **HAVE RESULTED IN LOWER INTEREST COSTS COMPARED**
20 **TO FINANCINGS THAT DID NOT EMPLOY BEST PRACTICES?**

21 A. One of the first regulatory authorities to employ the best practices
22 in question was the Public Utilities Commission of Texas (PUCT).

1 During the period from 2001 through 2006, there were six utility
2 securitizations completed in Texas with a total of 26 individual
3 tranches with WALs from 1.9 to 13 years. Each of those
4 transactions followed best practices as required by the PUCT.
5 During that same period, there were 18 transactions outside of
6 Texas which generally did not follow some or all of the best
7 practices required in Texas. Exhibit 2 shows how all of those
8 tranches were priced. The two regression lines demonstrate that,
9 on average, the Texas tranches priced significantly better (i.e.,
10 lower spreads to the swap benchmark and therefore lower interest
11 rates) compared to the non-Texas tranches.

12 **Q. IS THERE A WAY OF QUANTIFYING THE SAVINGS SHOWN**
13 **IN CHARTS SUCH AS EXHIBIT 2?**

14 A. Yes. Exhibit 3 is an analysis done by Citigroup in 2003 estimating
15 interest savings from the first three utility securitizations done
16 using best practices in Texas between 2001 and 2003 and
17 comparing them to all utility securitizations done between 1997
18 and 2003, graphically comparing securitization pricing spreads to
19 swaps, U.S. Treasury bonds, and credit card securitizations. The
20 study quantifies interest savings based on the swap spread pricing
21 difference between the Texas deals and all other deals. The study
22 calculates a total present value interest savings for the three
23 Texas deals of \$7,533,476. Subsequently, Citigroup reran its

1 analysis using a shorter time span, I believe it was 2001 to 2003,
2 and calculated NPV savings of about \$17 million (nominally \$23
3 million) for the same three Texas deals. These were the three
4 transactions which witness Rebecca Klein oversaw as Chair of the
5 PUCT, and Saber Partners served as financial advisor to the
6 PUCT for each of these three transactions.

7 **Q. HOW CAN THE SAVINGS CALCULATION BE SO DIFFERENT**
8 **FOR THE SAME THREE TRANSACTIONS?**

9 A. The differences in the savings calculation result from the fact that
10 savings estimates are sensitive to the time period over which the
11 comparisons are made. Generally, the more stable interest rates
12 are over the comparison period, the more valid the comparisons
13 are, since spread relationships change over time, independent of
14 how well any particular pricing is executed. Exhibit 4 shows how
15 swap spreads changed dramatically during the financial crisis of
16 2008 and 2009.

17 **Q. IS THERE ANY OTHER WAY OF MEASURING PRICING**
18 **PERFORMANCE BESIDES COMPARING PRICING WITH**
19 **BENCHMARK SWAP SPREADS?**

20 A. Yes, there is, especially after the financial crisis of 2008 and 2009.
21 Exhibit 4 shows pricing spreads to swaps for tranches in the range
22 of nine- to 10-year WAL from 2001 to 2012. There are two
23 important points to note from this chart. First, from 2001 through

1 2007, transactions in which Saber Partners acted as financial
2 advisor following best practices led the march toward tightening
3 spreads, as every deal had tighter spreads than the preceding
4 deal. The second point is that with the financial crisis of 2008-2009
5 and its aftermath, pricing spreads to swaps widened dramatically,
6 and only partially recovered in the years after. It seems apparent
7 that, with spreads changing so substantially over short periods of
8 time, it would be misleading to try to compare performance of one
9 deal to others if the deals were more than a year or two apart. We
10 believe the solution is to do what is called relative value
11 benchmarking with types of securities that price closer to utility
12 RBBs than either U.S. Treasury bonds or swaps.

13 **Q. PLEASE EXPLAIN WHAT YOU MEAN BY “RELATIVE VALUE**
14 **BENCHMARKING.”**

15 A. Exhibit 5 is a paper that I authored explaining in detail what we
16 mean by relative value benchmarking and how it works. Basically,
17 it involves looking at a range of types of securities that are, at least
18 in some way, comparable to utility RBBs. These might include
19 AAA-rated corporate bonds such as Johnson & Johnson (JNJ)
20 and Microsoft (MSFT). It could include AAA-rated credit card
21 securitizations, which are in fact asset-backed securities. It could,
22 and in fact should, include AAA-rated U.S. agency debt by such
23 issuers as Fannie Mae (FNMA), Federal Home Loan Bank

1 (FHLB), or the Tennessee Valley Authority (TVA). The basket of
2 comparables could even include some electric utility debt, even
3 though there are no AAA-rated utilities. By comparing yields on
4 these types of securities to the indicative rates provided by the
5 underwriters in the weeks and days leading up to pricing, the
6 issuer can get a good sense of the reasonableness of those
7 indicative rates. For example, if the indicative spreads on the
8 RBBs would result in a higher yield than on electric utility corporate
9 debt, then there is definitely something wrong with the price
10 indications given by the underwriters.

11 **Q. YOU HAVE EXPLAINED HOW RELATIVE VALUE**
12 **BENCHMARKING IS USED LEADING UP TO PRICING. HOW**
13 **CAN IT BE USED AFTER PRICING TO MEASURE THE**
14 **SUCCESS OR FAILURE OF PRICING RELATIVE TO OTHER**
15 **SECURITIZATION TRANSACTIONS?**

16 A. Each of the types of comparable securities listed in my previous
17 answer is imperfect in some way as a measure of pricing
18 performance; JNJ and MSFT because they are the only two
19 corporate AAAs; credit card securitizations because they do not
20 exist for longer maturities and because they carry prepayment risk
21 that utility securitization debt does not; U.S. agency securities
22 because it would be easy to cherry-pick the best debt issues

1 among them so as to make a particular utility securitization pricing
2 look good in retrospect.

3 **Q. WHAT IS THE SOLUTION TO THESE PROBLEMS?**

4 A. The solution is to use U.S. agency debt, but to let an unbiased
5 third party pick the particular debt issues among all the U.S.
6 agency debt securities outstanding. This avoids the possibility of
7 so-called cherry picking to make a particular pricing look good or
8 bad according to one's bias. In this case, the unbiased third party
9 is the Bloomberg Terminal, a computer software system that
10 provides financial information and data to financial professionals
11 in all major corporations. The data include both current and
12 historical prices and yields for a seemingly infinite variety of debt
13 and equity securities. In addition to publishing prices and yields on
14 individual debt issues, Bloomberg publishes a yield curve for U.S.
15 agency debt, for which it picks specific agency issues for various
16 maturities along the curve. These data can then be used to
17 calculate spreads at the time of pricing any particular utility
18 securitization. This yield curve is called the I-26 Agency Curve.
19 Securitization spreads can be calculated to interpolated agency
20 yields in the same way that they are calculated to interpolated U.S.
21 Treasury bond yields.

22 **Q. WHY IS IT BETTER TO USE SPREADS TO U.S. AGENCY DEBT**
23 **AS A MEASURE OF PERFORMANCE RATHER THAN**

1 **SPREADS TO SWAPS AS WAS DONE IN EXHIBITS 2, 3, AND**
2 **4?**

3 A. Before the financial crisis of 2008-2009, it would not have made
4 much difference which benchmark was used. However, as Exhibit
5 4 shows, the crisis caused the relationship between swaps and
6 utility securitization debt to change significantly. While the
7 relationship between U.S. agency debt and securitization debt
8 also changed, the effect was much smaller. The relative changes
9 can be seen in Exhibit 6, which shows the securitization spreads
10 to swaps and spreads to U.S. agency debt for all utility
11 securitizations in the years before and after the financial crisis.
12 The charts show the relative stability of the two relationships by
13 comparing the standard deviations in each case. In the period
14 before the financial crisis, the standard deviation for spreads to
15 swaps (15.8 basis points (bps)) was almost the same as for
16 spreads to U.S. agency debt (14.8 bps). However, after the crisis,
17 the standard deviation for swaps increased dramatically to 25.6
18 bps, while for U.S. agency debt, it decreased slightly to 13.7 bps.
19 When attempting to measure relative success of one utility
20 securitization against others, it is necessary to compare
21 transactions that occurred in particular time periods. Therefore, a
22 good benchmark for this purpose is one that is more stable over
23 time. Exhibit 6 supports the conclusion that the spreads to U.S.

1 agency debt as measured by interpolated yields from the
2 Bloomberg I-26 curve are more stable with less variability and
3 therefore a better measure than swap spreads.

4 **Q. BESIDES USING A DIFFERENT BENCHMARK SECURITY, DO**
5 **YOU GENERALLY FOLLOW THE METHODOLOGY USED IN**
6 **THE CITIGROUP ANALYSIS TO CALCULATE INTEREST**
7 **SAVINGS FROM FOLLOWING BEST PRACTICES?**

8 A. Generally, yes. We calculate both nominal and NPV savings after
9 each financing for which we act as advisor, comparing that pricing
10 of that transaction to securitizations that have priced in the
11 recently preceding years for which we did not act as advisors. We
12 focus on NPV savings since they are more relevant to the financial
13 interests of the ratepayer than nominal savings, taking into
14 account the time value of money. Unlike the Citigroup analysis, we
15 do the analysis for each transaction we complete individually so
16 that each deal has its own set of comparable deals. Citigroup, on
17 the other hand, used a single group of comparable deals to
18 evaluate all three Texas deals.

19 **Q. WHAT INTEREST RATE DO YOU USE TO DISCOUNT**
20 **INTEREST SAVINGS?**

21 A. We have come to the conclusion that the petitioning utility's overall
22 weighted average cost of capital (WACC) is the best proxy for the
23 ratepayers' cost of capital. That is, in my opinion, the theoretically

1 correct rate to use, since securitization debt is a direct obligation
2 of the ratepayers and not the utility. In the present case, DEC and
3 DEP are discounting at the after-tax WACC, which is below both
4 the pre-tax and the overall WACC. I don't believe it makes a
5 material difference in this proceeding which WACC is used. Many
6 utility commissions choose to use the RBB rate to discount interest
7 savings, which is much lower and which I believe likely overstates
8 interest savings from the ratepayers' perspective.

9 **Q. CAN YOU SHOW AN EXAMPLE OF THE APPLICATION OF**
10 **YOUR APPROACH TO CALCULATING INTEREST SAVINGS**
11 **IN A UTILITY SECURITIZATION POST FINANCIAL CRISIS?**

12 A. Yes. The DEF nuclear asset recovery issue priced on 6/15/2016.
13 Exhibit 7 shows how the five series priced relative to all other utility
14 securitizations from 2010 to 2016 in terms of spreads to the
15 Bloomberg I-26 U.S. agency bond yield curve. The chart shows
16 that the first three series, with WALs of two, five, and ten years,
17 respectively, priced almost exactly on the regression line for all
18 other transactions in that timeframe. However, the two longer
19 series, with WALs of 15.2 and 18.7 years, respectively, priced well
20 below the regression line. The difference between the regression
21 line, which you could consider as average pricing performance,
22 and the actual spread to U.S. agency bonds represents interest
23 savings to the ratepayers. Discounted at DEF's WACC at that time

1 of 8.12%, the NPV savings for ratepayers amounts to over \$6.8
2 million.

3 **Q. DOES THIS MEAN THAT IN THE FUTURE, WHEN YOU PRICE**
4 **THIS TYPE OF SECURITY, THE AGREED-UPON PRICE WITH**
5 **THE UNDERWRITERS WILL BE BASED ON A SPREAD TO**
6 **U.S. AGENCY BONDS RATHER THAN A SPREAD TO SWAPS**
7 **OR SPREAD TO U.S. TREASURY BONDS?**

8 A. No, it does not. When setting the final pricing of such securities,
9 we must follow the market convention, which dictates that the
10 pricing be stated either as a spread to swaps or a spread to
11 interpolated U.S. Treasury bonds. However, for negotiating prior
12 to that point as well as for evaluating performance after the deal is
13 done, in my judgment U.S. agency securities represent the best
14 relative value benchmark among all the comparable debt types.

Savings Through Structural Changes

15 **Q. YOU STATED PREVIOUSLY THAT THERE IS A SECOND**
16 **DETERMINANT THAT CAN HAVE A LARGE IMPACT ON**
17 **RATEPAYER SAVINGS, NAMELY THE STRUCTURE OF THE**
18 **SRB. PLEASE GIVE AN EXAMPLE OF HOW A STRUCTURAL**
19 **CHANGE MIGHT INCREASE SAVINGS.**

20 A. In the 2016 DEF securitization, as witness Heller relates in his
21 testimony, at the suggestion of the Florida Public Utilities

1 Commission's financial advisor, the planned four-tranche structure
2 was changed to a five-tranche structure about a week before final
3 pricing. The original 16.9-year 4th tranche of about \$525 million
4 was split into two smaller tranches. The A-4 tranche became a
5 15.2-year WAL, \$250 million tranche and the A-5 tranche was
6 created as an 18.7-year WAL, \$275 million tranche. The original
7 A-4 tranche was quoted by the bankers with a g-spread (spread
8 to US Treasuries) of 117 basis points (1.17%). The final pricing of
9 the two new tranches was a 103 basis point spread on the new A-
10 4 tranche and a 116 basis point spread on the new A-5 tranche.
11 This resulted in 14 basis point savings on \$250 million and one
12 basis point savings on \$275 million. This created an additional
13 NPV savings of over \$3 million by just one small structural change
14 that affected neither the total principal amount, nor the overall
15 WAL life of the transaction.

16 **Q. ARE THERE OTHER TYPES OF STRUCTURAL CHANGES**
17 **THAT MIGHT PRODUCE SIGNIFICANT INCREMENTAL NPV**
18 **SAVINGS FOR RATEPAYERS?**

19 A. Yes. In witness Heath's testimony, he suggests that the
20 Companies prefer a 15-year amortization period for the bonds
21 because it "strikes the right balance between the length of the
22 recovery period and the length and level of the recovery charge."
23 Witness Heath also states that this is consistent with the longest

1 recovery period proposed by Public Staff in the DEP storm deferral
2 docket (Docket No. E-2, Sub 1193). He says that DEC and DEP
3 also considered a 20-year final payment date, but presents no
4 data in his direct testimony to show the effect of extending the
5 scheduled final maturity from 15 to 20 years. In response to DR 5-
6 1, spreadsheets provided by witness Abernathy show that such an
7 extension would increase NPV savings to ratepayers by over \$63
8 million total between DEC and DEP.

Problems with Testimony of Abernathy and Atkins

9 **Q. WHAT DID YOUR REVIEW OF THE INTEREST RATE**
10 **ASSUMPTIONS USED IN WITNESS ABERNATHY'S**
11 **CALCULATION OF SAVINGS FOR THE 20-YEAR STRUCTURE**
12 **REVEAL?**

13 A. I found two significant but more or less off-setting errors in the
14 interest rates used in the calculation.

15 **Q. WHAT WAS THE FIRST ERROR?**

16 A. First, as with the savings calculation for the 15-year scheduled
17 final structure, Ms. Abernathy relied on an overall interest rate that
18 was weighting coupons of five tranches by principal amount but
19 ignoring the WAL of each tranche, thus significantly understating
20 the true overall rate. It is incorrect to weight the individual coupon
21 rates just by the principal amounts of the respective tranches.

1 They must also be weighted by their respective weighted average
2 lives, since obviously an interest rate on Atkins' 18.1-year tranche
3 has more impact overall than the same interest rate on a 1.7-year
4 tranche. It appears that she got her overall rate of 1.51% from a
5 spreadsheet, also attached to response to DR 5-1 but provided by
6 witness Atkins, which contains rates for the individual 5 tranches.
7 The correct weighted average interest rate using Atkins' individual
8 rates for the 5 tranches on the 20-year scheduled final structure
9 would be 1.83%.

10 **Q. WHAT IS THE SECOND ERROR?**

11 A. Witness Atkins obtained his rates for the individual tranches from
12 Guggenheim. I have taken the rates he used in his direct testimony
13 and in his responses to two data requests, PS DR 5-1 and PS DR
14 9-2, for both the 15-year and the 20-year final scheduled maturity
15 structure and plotted them in Exhibit 8. The graph shows that the
16 rates for all the tranches fall, more or less, along a trendline above
17 the yield curve for US Treasury bonds yields, with two obvious
18 exceptions. The biggest outlier from the PS DR 5-1 response is
19 the A-5 tranche in the 20-year scheduled final maturity structure
20 with a WAL of 18.1 years, to which he assigns a rate of 2.54%,
21 which is 101 basis points above the interest rate of the next closest
22 tranche at 14 year-WAL with a rate of just 1.53%. The A-5 tranche
23 appears to be overstated by at 50 to 75 basis points (0.50% to

1 .75%) when compared to the trendline of all other interest rates
2 provided by witness Atkins for the various tranches in his direct
3 testimony and in response to PS DR 5-1.

4 **Q. SUBSEQUENT TO RESPONDING TO PS DR 5-1, DID**
5 **GUGGENHEIM OR WITNESS ATKINS CHANGE THEIR**
6 **ESTIMATE OF THE A-5 TRANCHE INTEREST RATE?**

7 A. No. In PS DR 9-2.m, the following question was asked in hopes
8 that the error would be corrected: "In response to PS DR 5-1, there
9 is an attached excel spreadsheets showing witness Atkins'
10 assumed interest rates for a 20-year SRB structure in which the
11 A-4 14-year tranche has an interest rate of 1.53%, equating to a
12 g-spread of about 50 basis points, whereas the A-5 18.1-year
13 tranche has an interest rate of 2.54%, equating to a g-spread of
14 about 130 basis points. Please explain why the DEC/DEP believes
15 that the 4 additional years of weighted average life for that tranche
16 should cause such a large increase in credit spread given the
17 slope of the US Treasury benchmarks?" However, rather than
18 reduce the rate for the A-5 tranche, the answer given by Witness
19 Atkins was to raise the rate for the A-4 tranche, in the following
20 response: "The exhibit to the response to PS DR 5-1 contained a
21 clerical error in the estimated spreads as of October 9, 2020 that
22 affected the spread and the yield of the A-4 tranche. The corrected
23 estimated spreads that were intended to be provided are in the

1 attachment provided with this response.” The rate for A-4 shown
2 in the excel attachment was 1.88%, up from 1.53%. As shown in
3 my Exhibit 8, now both the A-4 and the A-5 rates in Atkins’ 20-yr.
4 scheduled final maturity structure are significantly above the
5 trendline established by his rates for the 15-year scheduled final
6 maturity structure as well as the first three tranches of his 20-year
7 scheduled final maturity structure.

8 **Q. TO WHAT WOULD YOU ATTRIBUTE THE CAUSE FOR SUCH**
9 **OUTLIER RATES?**

10 A. I believe they are either a result of a carelessness or possibly an
11 indication of underwriters’ natural inclination to favor shorter
12 maturities because they are easier to sell. In either case, it would
13 appear that witness Atkins did not seriously consider the 20-year
14 scheduled final maturity structure as an alternative to the
15 Companies’ preferred 15-year scheduled final maturity structure.

16 **Q. ARE THERE, IN YOUR OPINION, ANY FINANCIAL OR NON-**
17 **FINANCIAL REASONS FOR OR AGAINST EXTENDING THE**
18 **SCHEDULED FINAL MATURITY BEYOND 15 YEARS?**

19 A. Yes, for both. The argument against extending could be based on
20 a belief that major storms were going to begin to occur much more
21 frequently and a desire to avoid “pancaking” capitalized O&M, one
22 storm after another, i.e., accumulating charges from multiple new
23 storms before the charges for old storms are completely paid.

1 However, there are several arguments for extending the maturity.
2 First, in the traditional case presented by witness Abernathy, she
3 assumes that capitalized O&M is financed over 15 years but the
4 storm-related capital piece is depreciated over 40 years. If we
5 were to take the weighted average of those two maturities based
6 on the principal amounts financed with SRBs, the maturity would
7 be slightly less than 18 years. Increasing the securitization final
8 scheduled maturity by just three years increases NPV savings by
9 about \$40 million for DEC and DEP combined, assuming the
10 principal amount financed in Atkins Exhibit 4.

11 The second argument supporting a longer maturity with SRBs is
12 simply that interest rates are within half a percent of the lowest
13 they have been in the last century or more. Consequently, it is in
14 both the ratepayers' and the utilities' interest to take full advantage
15 of such low rates for as long as reasonably possible. After all, there
16 are very few ratepayers who could borrow funds for less than 2%,
17 as they would effectively be doing with SRBs.

18 **Q. WHAT OTHER KINDS OF STRUCTURAL CHANGES MIGHT**
19 **HAVE SIGNIFICANT FINANCIAL IMPACTS?**

20 A. Witness Atkins suggests that employing a grantor trust structure
21 to combine the DEC and DEP bonds into a single bond offering
22 would avoid what, in his opinion, might be a financial penalty for
23 the smaller deal size of the DEC bond offering.

1 **Q. DID WITNESS ATKINS OFFER ANY EVIDENCE THAT SUCH A**
2 **PENALTY ACTUALLY EXISTS FOR SMALLER OFFERINGS?**

3 A. In his response to a data request, PS DR 2-8, he pointed to two
4 paired securitization offerings, one in 2010 and the other in 2014,
5 in which in each case a smaller offering was sold at the same time
6 as a larger offering by different but related sponsoring utilities. He
7 stated that in both cases, the smaller offering was priced with a
8 higher interest rate than the larger. However, my review of his
9 quantitative analysis indicates that it was not done correctly, and
10 thus does not support his contention.

11 **Q. PLEASE EXPLAIN THE NATURE AND CONSEQUENCES OF**
12 **THIS ERROR.**

13 A. In his PS DR 2-8 Supplemental attachment, Witness Atkins
14 compares a \$468.9 million Louisiana ELL (Entergy Louisiana,
15 LLC) deal with a \$244.1 million Louisiana EGSL (Entergy Gulf
16 States Louisiana, LLC) deal, both priced on 7/15/2010 with the
17 same WAL of 6.6 years. He calculates overall interest rates of
18 2.795% for the larger ELL deal and 2.819% for the smaller EGSL
19 deal for a difference of 2.4 basis points per annum or .024%
20 penalty per annum for the smaller deal. However, it is incorrect to
21 weight the individual coupon rates only by the principal amounts
22 of the respective tranches. They must also be weighted by their
23 respective WALs, since obviously an interest rate on a 10-year

1 WAL tranche has greater impact overall than the same interest
2 rate on a two-year WAL tranche. When the interest rates are
3 weighted correctly by principal and WAL, the “penalty” for the
4 smaller deal is just 1.57 basis points or .0157%, as shown in
5 Exhibit 9. That difference costs the smaller \$244 million deal just
6 \$253,000 in additional interest.

7 The consequence of witness Atkins’ error is greater in the 2014
8 deals. There, he compares a \$243.85 million Louisiana ELL deal
9 to a \$73 million Louisiana EGSL deal, both priced on 7/29/2014
10 with a WAL of 6.7 years. His attachment shows an overall rate of
11 2.646% for the larger deal compared to 2.860% for the smaller
12 deal for an apparent size penalty of 21.4 basis points or .214%.
13 However, in this case, when the correct rates weighted by both
14 principal and WAL are used, the larger deal has an overall interest
15 rate of 2.9732%, also shown in Exhibit 9, which is 11 basis points
16 or .11% more expensive than the smaller deal, contradicting
17 Atkins’ hypotheses that smaller transactions tend to suffer pricing
18 penalties. That means that the smaller \$71 million deal saved over
19 half a million dollars in interest by pricing lower than the larger
20 deal.

21 This result seems to impeach Witness Atkins’ rationale for using
22 the more complex and more expensive grantor trust structure to
23 sell the DEC and DEP bonds under a single structure.

1 **Q. WAS THERE A DATA REQUEST TO WITNESS ATKINS**
2 **QUESTIONING THE WAY HE CALCULATED WEIGHTED**
3 **AVERAGE INTEREST RATES?**

4 A. Yes. PS DR 8-3 asked, “Please provide the weighted average
5 interest rate for each of the four (4) transactions, weighted by
6 principal amount and weighted average life of the tranches in the
7 respective 4 transactions. If witness Atkins did not base his
8 conclusion that ‘the smaller transaction priced wider’ upon such
9 weighted average rates, then please explain what it was based on
10 and provide supporting data”. The response stated “Please see
11 the Companies' original and supplemental responses to PS DR 2-
12 8”. The original response to PS DR 2-8.a stated “Please see the
13 attached spread and coupon information for those transactions
14 included as an attachment to PS Data Request 2-8”, again
15 referring to the four Louisiana transactions. However, there was
16 no such attachment. Subsequently, witness Atkins submitted PS
17 DR 2-8 Supplemental, which had an attachment containing the
18 weighted average interest rates, weighted by principal but not by
19 WAL. He did not explain why he thought that was appropriate to
20 not consider WAL.

21 **Q. ARE THERE OTHER UTILITY SECURITIZATIONS THAT**
22 **MIGHT TEND TO DISPROVE ATKINS' CONTENTION?**

1 A. Yes. In 2007 and again in 2009, Allegheny Power priced a pair of
2 securitizations for each of two subsidiaries, Monongahela Power
3 (MP Environmental Funding) and Potomac Edison (PE
4 Environmental Funding). In each case, the two issuers priced with
5 the same spreads even though the PE deal was about 1/3 the size
6 of the MP deal. Exhibit 10 shows the 2009 deals priced better than
7 expected when compared to two other utility securitizations in the
8 same time frame.

9 **Q. ARE THERE ANY OTHER INSTANCES WHERE WITNESS**
10 **ATKINS' MISCALCULATION OF THE WEIGHTED AVERAGE**
11 **INTEREST RATE MAY BE CAUSING ERRONEOUS OR**
12 **MISLEADING RESULTS?**

13 A. Yes. In Exhibit 4 to Witness Atkins' direct testimony, he presents
14 preliminary structures for the DEC and DEP transactions showing
15 five tranches with five interest rates with a resulting overall interest
16 rate of 1.15%. If he were to calculate the weighted average rate
17 correctly, it would be about 1.38% or 23 basis points higher. Since
18 Witness Abernathy is using Mr. Atkins' overall rate in her savings
19 calculation, she consequently overstates the savings.

20 **Other Changes to the Proposed Financing Order**

21 **Q. ARE THERE ANY OTHER CHANGES TO THE COMPANIES'**
22 **PROPOSED FINANCING ORDER THAT YOU WOULD**

1 **SUGGEST THAT WOULD RESULT IN MATERIAL**
2 **RATEPAYER SAVINGS?**

3 A. There are several, which involve charges during the life of the
4 bonds and also collections after the bonds mature. At least four
5 utility commissions in eight RBB transactions between 2005 and
6 2014 have limited earnings of the sponsoring utility on the capital
7 subaccount to actual investment returns on the account, rather
8 than requiring ratepayers to provide a return equal to the rate on
9 the longest tranche, as stated in the Companies' proposed
10 Financing Order. This change from the proposed Financing Order
11 would save the Companies' ratepayers, taken together, nominally
12 about \$1.2 million over 15 years and on an NPV basis, about
13 \$500,000. The funds are in a AAA subsidiary primarily for tax
14 purposes and if used at any point, it is trued up immediately thru
15 the storm recovery charge on ratepayers on a constant basis. It
16 also is returned to the Companies upon the final maturity of the
17 bonds. The Companies' capital is not at risk, and thus there is no
18 justification in this instance for a higher return to the Company,
19 charged to the ratepayers, than actually earned on the account
20 itself. The Companies should be allowed to collect no more than
21 the actual investment return on the capital subaccount, which is in
22 addition to the other considerable benefits that they will receive
23 from doing this securitization.

1 **Q. WHAT BENEFITS, SPECIFICALLY, ARE YOU REFERRING**
2 **TO?**

3 A. Under traditional ratemaking as practiced by this Commission,
4 there is usually a gap between the date of the storms and the next
5 general rate case. In those instances, the amortization and the
6 carrying costs are typically presumed to be recovered in existing
7 rates during the interim period of time. Under the securitization
8 statute, that is not the case; amortization does not begin until the
9 bonds are issued, and the Company gets to accrue carrying costs
10 up to that date. So, use of securitization under these
11 circumstances ultimately increases the revenue collected by the
12 Company from the ratepayers by deferring for future collection
13 many millions of dollars from at least a year's worth of "gap period"
14 amortization and carrying costs.

15 **Q. Will the Companies and their SPEs continue to collect storm**
16 **recovery charge revenues after all the storm recovery bonds**
17 **have been repaid?**

18 A. Yes. Customers will no longer be obligated to pay the storm
19 recovery charge in respect of electricity consumed after all the
20 storm recovery bonds have been repaid. But customers still will be
21 obligated to pay storm recovery charges in respect of electricity
22 consumed through the date on which all storm recovery bonds

1 have been repaid. We sometimes refer to these amounts as “tail-
2 end collections.”

3 **Q. Can you estimate the amount of tail-end collections in**
4 **connection with the proposed storm recovery bonds?**

5 A. Yes. Based on assumptions used in the model embedded in the
6 testimony of witness Byrd’s Exhibit 1 and the Companies’
7 collection curves provided in response to PS DR 3-2.b, the
8 Companies and their SPEs would receive approximately \$20
9 million of tail-end collections. In one way or another, these excess
10 collections should be credited back to ratepayers.

11 **Q. The proposed form of Financing Order attached as Appendix**
12 **C to the Joint Petition calls for (i) servicing fees and**
13 **administration fees collected by the Companies to be**
14 **included in the Companies’ cost of service, (ii) the**
15 **Companies to credit back all periodic servicing fees in excess**
16 **of the Companies’ incremental costs of performing servicing**
17 **and administrative functions, and the expenses incurred by**
18 **the Companies to perform obligations under the Servicing**
19 **Agreement or Administration Agreement not otherwise**
20 **recovered through the storm recovery charge to be included**
21 **in the Companies’ cost of service “in the next rate case.” Why**
22 **is this crediting necessary?**

1 A. In the absence of crediting future rates or some other use of these
2 fees received by the Companies in excess of their costs incurred
3 in providing these services, the Companies would recover the
4 same costs twice from customers. Using witness Heath's
5 estimated cost of serving fees of .05 percent of the original
6 principal amount per year, that amounts to \$489,400 per year or
7 in excess of \$7 million over 15 years for the Companies combined.

8 **Q. Does the proposed form of Financing Order also call for "tail-**
9 **end collections" of storm recovery charges to be credited**
10 **back to customers in the Companies "next rate case"?**

11 A. Yes. Page 41 states: "Upon the maturity of the Storm Recovery
12 Bonds and upon the discharge of all obligations with respect to
13 such bonds, amounts remaining in each Collection Account will be
14 released to the appropriate SPE and will be available for
15 distribution by the SPE to DEP. As noted in this Financing Order,
16 equivalent amounts, less the amount of any Capital Subaccount,
17 will be booked to a regulatory liability and credited back to
18 customers in the Company's next rate case following the maturity
19 of the Storm Recovery Bonds."

20 **Q. Have commissions in other states devised other mechanisms**
21 **to provide greater protection for customers against such**
22 **overcollections of securitization charges?**

- 1 A. Yes. In 2006, FPL applied to the FPSC for a Financing Order
2 authorizing securitized storm recovery bonds to be issued for FPL.
3 Much of the proceeds of those storm recovery bonds were to be
4 used to fund additions to an existing Storm and Property
5 Insurance Reserve Fund (Reserve) which had been established
6 in 1993 to implement a self-insurance approach to storm costs
7 through annual contributions from base rate revenues. In the
8 Financing Order authorizing the issuance of storm recovery bonds
9 for FPL, the FPSC found that:
- 10 • FPL had not justified that the annual fees for servicing and
11 administration services was necessary to cover any incremental
12 costs to be incurred by FPL in performing those services.
13 Consequently, the FPSC “ORDERED that FPL shall apply to the
14 Reserve all amounts it will receive under the Servicing Agreement
15 for ongoing services and that FPL shall apply to the Reserve all
16 amounts it will receive under the Administration Agreement for its
17 services.” and
 - 18 • “Upon the maturity of the storm-recovery bonds and upon
19 discharge of all obligations in respect thereof, remaining amounts
20 in the Collection Account will be released to the SPE and will be
21 available for distribution by the SPE to FPL. Equivalent amounts,
22 less the amount of the Capital Subaccount and earnings thereon,
23 will be credited by FPL to current customers’ bills in the same

1 manner that the charges were collected, or through a credit to the
2 Reserve or the capacity cost recovery clause if the Commission
3 determines at the time of retirement that a direct credit to
4 customers' bills is not cost-effective. FPL shall similarly credit
5 customers an aggregate amount equal to any Storm Bond
6 Repayment Charges subsequently received by the SPE or its
7 successor in interest to the Bondable Storm Recovery Property."

8 **Q. Does providing these rate credits to customers "in the next**
9 **rate case" provide adequate and appropriate protection for**
10 **customers against overcollections by the Companies?**

11 A. As Public Staff witnesses Maness and Boswell state in their
12 testimony in this proceeding, the Companies historically have not
13 filed rate cases every year, and many years might pass before the
14 next rate case. For this reason, witnesses Maness and Boswell
15 recommend that the Commission's Financing Order (i) direct each
16 Company to establish two deferred accounts with respect to the
17 proposed storm recovery bonds: a "storm recovery bond excess
18 fees account" and a "storm recovery bond excess collections
19 account," (ii) provide that the positive or negative balance in each
20 of these deferred accounts, adjusted if appropriate for income
21 taxes and accrued carrying costs at the Companies' respective
22 net-of-tax weighted average cost of capital, and (iii) direct that the
23 balances in these deferred accounts be credited to customers in

1 an appropriate fashion in the next general rate case, without
2 regard to the historical base year used for that next rate case. The
3 recovery of the deferred credit may or may not be accompanied
4 by an ongoing credit to reflect continuing expected excess fees
5 and collections, subject to further true-up. I believe the approach
6 recommended by witnesses Maness and Boswell would provide
7 adequate and appropriate protection for customers against
8 overcollections by the Companies.

Summary and Recommendations

9 **Q. PLEASE BRIEFLY SUMMARIZE YOUR TESTIMONY.**

10 A. The market for utility securitization financing is not a 100% efficient
11 market and therefore it is important that the Commission or Public
12 Staff have an experienced representative with co-equal authority
13 with DEC and DEP following established best practices to act on
14 behalf of ratepayers in the structuring and pricing of the proposed
15 SRB financing. Without such expert representation, it is unlikely
16 that the bonds will meet the statutory requirement of lowest storm
17 recovery charge at the time the bonds are priced.

18 **Q. PLEASE LIST YOUR RECOMMENDATIONS FOR THE**
19 **COMMISSION.**

20 A. In general, the Commission should modify the proposed Financing
21 Order to allow for the Best Practices identified in my testimony as

1 well as that of witnesses Abramson, Maher and Klein, and
2 summarized by witness Fichera. Most importantly, the Financing
3 Order should provide that the Companies and the Public Staff,
4 together with its independent financial advisor, have equal
5 authority with respect to major decisions involving structuring,
6 marketing, and pricing of the proposed SRBs and selection of
7 underwriters and other transaction participants. Second, the
8 Financing Order should allow for a final scheduled maturity of up
9 to 20 years. Third, the Financing Order should contain provisions
10 that prevent excess charges, where possible or return excess
11 charges to the ratepayer in a timely fashion, if not. Finally, the
12 Commission should carefully evaluate the value of including the
13 grantor trust structure as an option in the Financing Order, given
14 its increased complexity and the lack of any evidence supporting
15 the value of such an option.

16 **Q. DOES THIS COMPLETE YOUR TESTIMONY?**

17 A. Yes, it does

1 Q. Mr. Sutherland, do you have a summary of your
2 testimony?

3 A. I do.

4 Q. Now, you filed with the Commission, a summary
5 a couple of days ago, and I believe you have a slight
6 correction in your summary.

7 When you get to that point, will you point it
8 out, what the correction is?

9 A. Yes, I will.

10 Q. Okay. Please proceed and give your summary.
11 Thank you.

12 A. The purpose of my testimony is to discuss and
13 demonstrate how ratepayers benefit from
14 ratepayer-backed bond financing, and more specifically,
15 ways in which the benefit can be measured and maximized
16 through optimal structuring and application of "best
17 practices" by a properly structured bond team.

18 My testimony focuses on the quantitative
19 analysis of structuring and pricing decisions. By
20 comparing past ratepayer-backed bond pricings, both
21 with and without best practices, and also by pointing
22 out some misleading testimony by Companies' witnesses,
23 my testimony demonstrates the importance of having on
24 the bond team expert representation on behalf of the

1 ratepayer.

2 With an undergraduate degree in electrical
3 engineering from Cornell University and an MBA from the
4 University of Chicago, I worked for over 20 years with
5 Florida Power & Light Company, primarily in the area of
6 corporate finance. I then spent another 20 years with
7 Saber Partners, LLC involved in 13 utility
8 securitization transactions raising over \$9 billion in
9 an advisory role to public utility commissions on
10 behalf of ratepayers. My particular role as senior
11 advisor has been in the area of quantitative analysis.

12 The biggest net present value, NPV, savings
13 in a utility securitization result from the fact that
14 rating agencies -- Moody's, S&P, and Fitch -- generally
15 treat utility securitization debt as off-balance sheet,
16 despite the fact that it may not be so for other
17 accounting or regulatory purposes. This is important
18 because utilities set their capital structure, that is
19 to say their ratio of debt to equity, based on what is
20 necessary to maintain an acceptable bond rating by the
21 credit rating agencies. This means that utilities can
22 issue securitization debt without having to issue a
23 similar amount of equity to maintain what the rating
24 agencies consider the proper debt-to-equity ratio.

1 Without the need for that amount of equity, there is no
2 associated income tax expense.

3 Another large contributor to NPV savings from
4 securitization comes from the fact that the revenue
5 requirements are generally structured to be levelized
6 like mortgage payments rather than declining as is the
7 case with traditional utility revenue requirements.

8 With these savings factors intrinsic to all
9 RBB financings in mind, there are two major aspects
10 with which the bond issuer has some ability to affect
11 the amount of additional ratepayer savings resulting
12 from a well-executed securitization financing. The
13 first is the interest rate on the bonds, and the second
14 is the structure of the financing.

15 Decisions on structure might include the
16 maturity or weighted average life of the bonds and the
17 number and size of tranches or series of bonds. Both
18 the interest rate and the structure are determined as
19 part of the pricing process of bond issuance.

20 Consequently, the extent to which the pricing process
21 results in savings is determined by the efforts of the
22 bond team prior to and at the time of pricing.

23 Interest rates are established based on a
24 spread in basis points, or hundredths of a percent, to

1 the rate on a benchmark security. By convention,
2 asset-backed securities, ABS, are generally priced
3 relative to the rate on interest rate swaps, while
4 traditional corporate debt is priced relative to U.S.
5 Treasury bond rates.

6 Utility securitization bonds have usually
7 been priced like ABS, based off spread to swaps, but
8 the Duke Energy Florida transaction in 2016 was priced
9 using a spread to U.S. Treasury debt. In either case,
10 the securitized debt should be priced relative to a
11 security of the same weighted average life. If there
12 is no such security, then it should be priced based on
13 an interpolated rate between the two nearest in years
14 benchmark securities.

15 While an issuer cannot control the interest
16 rate on the underlying benchmark security at any point
17 in time, the issuer has the ability to achieve
18 attractive spreads to benchmark rates by effective
19 marketing, educating investors about unusually
20 attractive aspects of the RBBs, and by exercising good
21 analytical and negotiating skills. However, in order
22 to achieve the lowest cost for the ratepayer, the bond
23 team should include a representative of Public Staff or
24 Staff's financial advisor, since that is who has the

1 greatest incentive to protect ratepayer interests.

2 This is most important with utility securitization
3 issues because, unlike conventional utility debt,
4 securitization debt is a direct obligation of the
5 ratepayer and not the utility.

6 Interest rate savings relative to other
7 securitization financings can be measured by comparing
8 pricing spreads to benchmark rates for transactions
9 over some reasonably stable period of time. Since the
10 comparisons must be for similar weighted average lives,
11 a regression line can be used showing spreads versus
12 weighted average lives and then used to predict pricing
13 spreads for any particular weighted average life
14 tranche. The outcome for a transaction following best
15 practices with active involvement of a ratepayer
16 representative can be compared to the predicted pricing
17 results based on all other securitizations in the same
18 general time frame to calculate the value, or the
19 interest rate savings, from such best practices.

20 In addition to spreads used at the time of
21 pricing, spreads to other AAA debt securities, such as
22 U.S. agency securities, for example, Federal Home Loan
23 Bank or Tennessee Valley Authority, can be used to
24 judge success, both at the time of pricing and

1 thereafter. Various exhibits in my direct testimony
2 illustrate such savings over a variety of transactions;
3 as for example, Exhibit 7, showing interest savings in
4 the Duke Energy Florida transaction in 2016 compared to
5 all other RBBs from 2010 through 2016, and the diagram
6 shows savings of approximately 30 basis points each on
7 the two longest tranches, which resulted in net present
8 value interest savings of \$6.8 million.

9 Sometimes additional savings can be generated
10 simply by changing the number or size of the tranches
11 in a securitization. An example is given from the Duke
12 Energy Florida securitization in 2016 when, at the
13 suggestion of the Commission's financial advisor, a
14 simple change from a four-tranche to a five-tranche
15 structure resulted in an additional \$3 million net
16 present value savings for ratepayers.

17 Another type of structural change involves
18 extending the final scheduled maturity of the
19 financing. In direct testimony, the Companies
20 recommended a 15-year final scheduled maturity for both
21 DEC and DEP, despite the fact that a 20-year structure
22 offers substantially greater net present value savings.
23 My testimony points out several problems with the
24 Companies' analysis of a 20-year alternative structure

1 and discusses why the Companies' financial advisor
2 seems inclined to be dismissive of such alternative.

3 In addition to including Public Staff and/or
4 their financial advisor as part of a bond team, there
5 are three other changes suggested in my testimony. The
6 first is to restrict the return on the capital
7 subaccount held and managed by the bond trustee to just
8 actual earnings on investments made in the account
9 rather than a return equal to the rate on the longest
10 tranche of the financing. The second recommendation is
11 to reflect in the financing order a requirement that
12 all so-called tail-end collections of securitization
13 revenues collected after the bonds have been paid off
14 will be credited back to the ratepayers. The final
15 recommendation is that, to the extent actual, marginal
16 servicing, and administration costs incurred by the
17 Companies -- and here there is a change in wording.
18 Delete the word "exceed" and insert the word "are less
19 than" the assumed annual fee, those amounts will also
20 be credited back to the ratepayer in a timely manner.

21 Because -- besides these three
22 recommendations, it is my recommendation that the
23 Public Staff and its financial advisor have equal
24 authority with the Companies regarding all major

1 decisions involving structuring, marketing, and pricing
2 the securities. Beyond that, the Commission should
3 allow best practices as described by witnesses Fichera
4 and other Public Staff witnesses.

5 This completes my summary.

6 MR. GRANTMYRE: The witness is available
7 for cross examination.

8 MR. CREECH: And I would like -- now
9 would be a good time to introduce witness Heller as
10 well, would it not?

11 CHAIR MITCHELL: It would. Please
12 proceed, Mr. Creech.

13 MR. CREECH: Thank you.

14 DIRECT EXAMINATION BY MR. CREECH:

15 Q. Good morning. Mr. Heller, are you there?

16 A. (Steven Heller) I apologize, I just unmuted.

17 Q. Good morning. Good morning.

18 Mr. Heller, can you please state your name
19 and address for the record?

20 A. Steven Heller, 3 Fairbanks Court, Woodbury,
21 New York.

22 Q. And you're testifying today on behalf of the
23 Public Staff; is that correct?

24 A. Correct.

1 Q. Did you cause to be filed in these dockets on
2 December 21, 2020, direct testimony consisting of
3 19 pages and no exhibits, corrections filed on -- to
4 that testimony on January 6, 2021, and further
5 revisions and fully memorialized testimony on
6 January 13, 2021?

7 A. Yes.

8 Q. Do you have any corrections to your
9 testimony?

10 A. There might be one minor correction. At one
11 point, there was a table listing seven previous
12 transactions that I'd worked on, and there were
13 references to that number six a couple of times in the
14 narrative. I then recalled an additional transaction
15 that was added to the table, but the places in the
16 narrative that mentioned six weren't corrected to
17 seven. So nothing with regarding the thrust of the
18 testimony, but those minor mistakes are still present.

19 Q. Thank you. And if you were otherwise asked
20 the same questions today, would your answers be the
21 same?

22 A. Yes.

23 MR. CREECH: Chair Mitchell, at this
24 time I would move that Mr. Heller's prefiled direct

1 testimony as corrected, and corrected here on the
2 stand, be copied into the record as if given orally
3 from the stand.

4 CHAIR MITCHELL: All right. Hearing no
5 objection, Mr. Creech, to your motion, the prefilled
6 direct testimony of witness Heller consisting of
7 19 pages as corrected today on the witness stand
8 shall be copied into the record as if delivered
9 orally from the stand.

10 MR. CREECH: Thank you.

11 (Whereupon, the prefilled corrected
12 direct testimony of Steven Heller was
13 copied into the record as if given
14 orally from the stand.)

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BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

Docket No. E-2, Sub 1262
Docket No. E-7, Sub 1243

In the Matter of		
Joint Petition of Duke Energy	)	DIRECT TESTIMONY OF
Carolinas, LLC and Duke Energy	)	STEVEN HELLER,
Progress, LLC Issuance of Storm	)	PRESIDENT OF ANALYTICAL
Recovery Financing Orders	)	AID, CONSULTANT TO SABER
	)	PARTNERS, LLC

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

Docket No. E-2, Sub 1262
Docket No. E-7, Sub 1243

Direct Testimony of
Steven Heller, President of Analytical Aid, and
Consultant to Saber Partners, LLC
December 21, 2020

INDEX TO DIRECT TESTIMONY OF STEVEN HELLER

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Structuring DEC/DEP Storm Recovery Bond Issuances So As To Be
Included in the Aggregate Bond Index as Asset Backed Securities (ABS)
Will Cost Ratepayers 18

Successful Precedents 19

INTRODUCTION

- 1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**
- 2 A. My name is Steven Heller. My business address is 3 Fairbanks Ct,
- 3 Woodbury, NY 11797
- 4 **Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR**
- 5 **POSITION?**

1 A. I am President of Analytical Aid, and a consultant to Saber Partners,
2 LLC, solely for purposes of evaluating this North Carolina
3 securitization petition.

4 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND**
5 **PROFESSIONAL EXPERIENCE.**

6 A. I have a B.A. (1981) from Union College in Computer Science /
7 Chemistry and an M.B.A (1983) in Finance from NYU. I have over 37
8 years of experience in structuring and analyzing real estate and non-
9 real estate asset backed securities (ABS) while being employed at
10 firms including Salomon Brothers, Merrill Lynch, Credit Suisse and
11 Andrew Davidson & Co. My real estate ABS experience includes well
12 over 100 residential mortgage, commercial mortgage and PACE
13 assessment financings. My non-real estate ABS experience has
14 included several dozen Student Loan, Auto, and Pharmaceutical
15 Royalty transactions.

16 I also have extensive experience with non- ABS transactions such
17 as Stranded Cost / Rate Reduction Bond or Ratepayer-Backed Bond
18 financings with investor-owned utility securitization like the
19 Companies. With respect to Ratepayer-Backed Bonds similar to the
20 storm recovery bonds proposed by the Companies, my experience
21 has included being structuring agent on the following six (6) AAA
22 (S&P and Fitch) and Aaa (Moody's) rated investor-owned utility
23 Ratepayer-Backed Bond transactions over 14 years:

- 1 1. **2016** \$1.294 Billion for Duke Energy Florida (Duke Energy
2 Florida Project Finance LLC)
- 3 2. **2009** \$64 million Monongahela Power (MP Environmental
4 Funding LLC)
- 5 3. **2009** \$22 million for Potomac Edison (PE Environmental
6 Funding LLC)
- 7 4. **2007** \$652 million for Florida Power & Light Storm Recovery
8 Bonds (FPL Recovery Funding LLC)
- 9 5. **2006** \$1.739 billion for AEP Texas Central (AEP Texas
10 Central Transition Funding II LLC)
- 11 6. **2005** \$115 million for West Penn Power (WPP Funding LLC)
- 12 7. **2005** \$1.851 billion for CenterPoint Energy (CenterPoint
13 Energy Transition Bond Company II, LLC)

14 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

15 A. I will discuss the function of the modeler and structuring agent of
16 Ratepayer-Backed Bonds and give some insight into the different
17 perspectives and objectives of the structuring agent when working
18 for an investment bank as opposed to when the structuring agent is
19 an independent member of the financing team.

20 In addition, except as otherwise defined in this testimony, terms have
21 the meanings assigned to them in the Glossary, attached as the final

1 exhibit to the testimonies of Public Staff witnesses Joseph Fichera
2 and Paul Sutherland.

3 **Q. WHAT INFORMATION DID YOU REVIEW FOR THIS**
4 **TESTIMONY?**

5 A. I reviewed the Companies Testimony and the descriptions of the
6 securities and the assumptions and other aspect of the proposed
7 structure to evaluate in generally accepted financial principles the
8 outcomes and conclusions put forth by the Companies. To evaluate
9 someone else's financial work product, one needs to understand
10 what they did, what are their assumptions, what variables can be
11 independently verified and why they did it so as to properly give an
12 informed opinion as to my conclusions. Consequently, I reviewed the
13 Companies Witness Atkins' testimony and responses to Data
14 Requests from Public Staff to familiarize myself with the Companies
15 basic assumptions regarding Ratepayer-Backed Bond securitization
16 and the methodology employed to determine whether it was
17 reasonable and accurate based on my professional experience in
18 similar situations. Correct financial analysis requires context as well
19 as calculations.

20 **Q. YOU HAVE BEEN THE STRUCTURING AGENT ON SIX UTILITY**
21 **RATEPAYER-BACKED BOND TRANSACTIONS, THREE WHILE**
22 **WORKING AT A WALL STREET FIRM AND THREE WITH YOUR**

1 OWN FIRM OVER THE PAST 16 YEARS AND ONE OF THOSE
2 WAS THE DUKE ENERGY FLORIDA RATEPAYER-BACKED
3 BOND TRANSACTION. DID YOU RECEIVE A REQUEST FOR
4 PROPOSAL FROM DEC/DEP FOR STRUCTURING ADVISOR IN
5 THIS TRANSACTION?

6 A. No, I did not.

7 HOW THE STRUCTURING AGENT/ADVISOR AFFECTS
8 RATEPAYER INTERESTS

9 Q. AS THE STRUCTURING AGENT ON THOSE SIX
10 TRANSACTIONS AND CURRENT TRANSACTIONS, DID YOU DO
11 ALTERNATIVE SCENARIO ANALYSES?

12 A. Yes. I have prepared analyses of timing of a transaction under
13 different market conditions and different bond structures and
14 requirements of the issuer and commission to help the decision-
15 makers make informed decisions regarding securitization bonds.

16 Q. AS THE STRUCTURING AGENT ON THOSE SIX
17 TRANSACTIONS AND BASED ON YOUR REVIEW OF THE
18 STATUS OF THE CURRENT PROPOSED TRANSACTION, DID
19 YOU PREPARE MANY MORE SCENARIOS ANALYSES TO
20 COMPARE COSTS TO THE RATEPAYER THAN THAT
21 PRESENTED BY DEC/DEP IN ITS TESTIMONY?

22 A. Yes. I would normally run a number of structures varying the number
23 of tranches and tranche sizes to target different average lives to see

1 which produced the lowest cost and largest NPV savings to
2 ratepayers.

3 **Q. WHAT DATA MUST BE PROVIDED WHEN STRUCTURING A**
4 **UTILITY SECURITIZATION/ RATEPAYER-BACKED BOND TO**
5 **COMPARE COSTS TO THE RATEPAYER IN ALTERNATE**
6 **SCENARIOS?**

7 A. Generally, the first step is obtaining data from the sponsoring utility
8 on the following:

- 9 1. Long-term demand forecast by customer class to the
10 expected final term of the financing
- 11 2. Historical collection curve by customer class
- 12 3. Targeted proceeds - how much money is to be raised
13 including all recoverable expenses
- 14 4. Allocation of financing cost by customer class
- 15 5. Targeted term (maturity) of financing
- 16 6. Targeted Settlement Date of initial offering
- 17 7. U.S. Treasury yield curve and assumed pricing credit spreads
18 for average lives of tranches of two years and up
- 19 8. Historical demand variance - actual six-month vs forecast six-
20 month

1 **Q. WITNESS ATKINS HAS PROPOSED A TRANCHE WITH A**
2 **WEIGHTED AVERAGE LIFE OF JUST 1.4 YEARS. WHY WOULD**
3 **YOU JUST LOOK AT THE TREASURY YIELD CURVE STARTING**
4 **AT 2 YEARS?**

5 A. In all the deals I've worked on, no charge goes on customers' bills
6 until after the settlement date of the financing. Applying class by
7 class collection curve means actual cash comes in with a delay after
8 billing. So, the deal doesn't reach a full monthly cashflow until several
9 months into the deal. We have gotten permission to start level
10 revenue exempting these early months (otherwise you'd need to
11 start with a higher per kwh charge and then drop it once you were 6
12 months in). There typically would just be enough cash receipts to pay
13 interest for the first 6-9 months and not enough receipts to cover
14 principal in an amount needed to achieve a significant class size with
15 less than an average life of 2 years.

16 **Q. AS THE STRUCTURING AGENT, HOW DO YOU PREPARE A**
17 **MODEL TO COMPARE COSTS TO THE RATEPAYER UNDER**
18 **DIFFERENT SCENARIOS?**

19 A. Using the data described above, an initial model can be set up that
20 provides the required amount of financing that is paid back over the
21 desired term using a charge per class determined by the model so
22 that when applied to the demand forecast and collected at the pace
23 of the collection curves for each class, allocates the cost of the

1 financing across classes as required by the allocation provided.
2 Scenarios are then modeled based upon alternative inputs for
3 targeted proceeds, cost allocation, and terms to determine the
4 structure with the lowest all-in cost of funds. Over the course of the
5 pre-pricing period of a bond offering, many deal structures will be
6 analyzed repeatedly as benchmark U.S treasuries and credit
7 spreads move around.

8 **Q. WERE YOU ABLE TO REVIEW ANY SCENARIO ANALYSES**
9 **PREPARED BY DEC/DEP OR PREPARE YOUR OWN**
10 **ADDITIONAL SCENARIO ANALYSES?**

11 A. No, not in any great detail, because the Companies have conducted
12 very limited analysis and only provided some of the basic data
13 needed for such a model.

14 **Q. COULD THIS MODELING BE CONDUCTED IN THIS CASE AS**
15 **PART OF A PRE-BOND ISSUANCE REVIEW PROCESS?**

16 A. Yes, the type of modeling I describe above can and should be
17 conducted as part of a pre-bond issuance review process to ensure
18 compliance with the requirement that that customer costs be
19 minimized and present value savings to customers maximized to the
20 extent possible.

1 **Q. WOULDN'T AN EXAMINATION OF ALTERNATIVES TO**
2 **MAXIMIZE PRESENT VALUE FOR RATEPAYERS BE**
3 **PERFORMED BY THE UNDERWRITER?**

4 A. No, generally not. The underwriter's model is generally just audited
5 for accuracy but not for policy objectives like minimizing the charge
6 on customers. This is an important distinction.

7 **CONFLICTS OF INTEREST WITH RATEPAYERS'S BEST**
8 **INTERESTS ARE CREATED WHEN AN UNDERWRITER IS**
9 **ALSO THE STRUCTURING AGENT**

10 **Q. YOU HAVE MODELED RATEPAYER-BACKED BOND DEALS AT**
11 **INVESTMENT BANKS AND AS AN INDEPENDENT MODELER.**
12 **WHAT DIFFERENCES HAVE YOU EXPERIENCED THAT ARE**
13 **RELEVANT FOR THE COMMISSION TO CONSIDER IN**
14 **EVALUATING THE COMPANIES BASE CASE?**

15 A. At an investment bank, my typical direction came from a syndicate
16 or trading desk with a subjective guidance on average life targets and
17 number of classes or tranches including scheduled maturities. The
18 objectives usually will be the easiest or fastest sale. The firm makes
19 its profits by executing transactions. It wants to do as many
20 transactions as possible during the fiscal year (compensation cycle)
21 with the least risk to the firm's capital. That usually means to price
22 securities to sell quickly so that other deals can get done.

1 When consulting to utilities with active Commission involvement and
2 an independent financial advisor, I have access to a full supply of
3 spreads for different average lives (and potentially payment
4 windows/ principal amortizations and scheduled maturities). So
5 instead of being told the structure to create, I had the opportunity to
6 evaluate a larger number of alternatives in order to discover the best
7 structure with the lowest cost of funds (highest present value
8 savings) for the ratepayer rather than the structure that is the most
9 advantageous to the underwriter and their sales and trading
10 departments.

11 **Q. BASED ON YOUR EXPERIENCE, WHEN AN INVESTMENT BANK**
12 **HAS SERVED AS THE STRUCTURING AGENT FOR A UTILITY**
13 **SECURITIZATION, HAS THE STRUCTURING AGENT**
14 **RECOMMENDED STRUCTURES THAT FACILITATED THE**
15 **QUICKEST SALE AND NOT NECESSARILY THE LOWEST**
16 **CHARGES TO THE CONSUMER RATEPAYER?**

17 A. Yes, that is correct.

18 **Q. COULD YOU PROVIDE AN EXAMPLE OF THIS?**

19 A. Yes. In the most recent Ratepayer-Backed Bond I modeled, for Duke
20 Energy Florida, the underwriters (which included Guggenheim
21 Securities) wanted a 4-tranche structure to provide larger tranches
22 sizes. This is similar to Witness Atkins' proposal to combine the

1 transactions simply to get a larger tranche size. However, the
2 commission's independent financial advisor (Saber Partners, LLC)
3 and the utility asked for alternatives to be examined. Through my
4 analysis (with credit spreads for the yield curve provided by the
5 underwriters) Saber Partners recommended a 5-tranche structure
6 that had sufficient tranche sizes and narrower principal payment
7 windows and had a lower all-in cost of funds to the ratepayer, and
8 that's the deal that went to market (after a modest amount of
9 resistance from the bank). Without an independent and experienced
10 financial advisor in the process, the underwriter's structure would
11 have been used and the other alternatives not examined.

12 **Q WITNESS ATKINS TESTIFIES THAT QUALIFYING STORM**
13 **RECOVERY BONDS FOR INCLUSION IN THE AGGREGATE**
14 **BOND INDEX AS AN ASSET-BACKED SECURITY SHOULD BE**
15 **A PRIME MOTIVATING FACTOR FOR STRUCTURING THIS**
16 **TRANSACTION. HAS THIS TOPIC EVER COME UP IN YOUR**
17 **DISCUSSIONS?**

18 A. No, not to my recollection.

19 **Q. ARE THERE ANY OTHER MATERIAL DIFFERENCES BETWEEN**
20 **STRUCTURING UNDER THE DIRECTION OF AN INVESTMENT**
21 **BANK/UNDERWRITER VERSUS AS AN INDEPENDENT**

1 **MODELER NOT EMPLOYED BY AN UNDERWRITER OF THAT**
2 **TRANSACTION?**

3 A. Yes. Additionally, the investment bank typically charges a fee for
4 structuring between \$300,000 and 500,000 and typically wants
5 access to the underwriting fees which are higher in amounts since
6 they are based on a percentage of the bond size and not a fixed fee.
7 This fee is roughly three to five times the fee that I accept, which I
8 believe is fair for the work involved. All transactions that I have
9 worked on have achieved a AAA rating from all three nationally
10 recognized rating agencies in the same amount of time as when I
11 was at Credit Suisse, and all transactions I have worked on were sold
12 to investors at tight spreads.

13 **Q. HOW IMPORTANT IS ACCURACY IN MODELING CUSTOMER**
14 **CHARGES TO ACHIEVING A AAA RATING WHILE ALSO**
15 **ACHIEVING THE LOWEST CUSTOMER CHARGE?**

16 A. It is very important in order to anticipate and respond to rating agency
17 concerns regarding sensitivity to changes in sales, write-offs and
18 other variables. Rating agencies provide stress scenarios which
19 specify stressed demand forecasts as well as stressed collections.
20 For each stress scenario, we have to model what the charge for each
21 class would be at each true up. This is simulated in the model as
22 accurately as it would be by the client doing the true up in the future
23 in response to changes in demand and collections.

1 **Q. DO YOU THINK THE MODELS DONE FOR RATEPAYER-**
2 **BACKED BOND TRANSACTIONS ARE PROPRIETARY WORK**
3 **PRODUCT LIKE A TRADE SECRET AS THE COMPANIES CLAIM**
4 **THAT GUGGENHEIM ASSERTS IN RESPONSE TO PS DATA**
5 **REQUEST 8-3 IV?**

6 A. No I do not. My model under contract to Duke Energy Florida for
7 example was used by the company and its underwriters without any
8 restriction,

9 This is how we operate. I've developed Ratepayer-Backed Bond
10 models over and over again. They get a little better each time and
11 make it easier to do the most frequent tasks 1) running stress
12 scenarios and 2) considering structural alternatives. But the basic
13 model is not terribly complicated. For each customer class, multiply
14 the load forecast by the charge per kilowatt hour to get the billing
15 amount. Apply historical collection curve to the billing amount to get
16 revenue received. That revenue is the source of payments of interest
17 and principal on the bonds. Now it's slightly more complicated in that
18 we modify the per kilowatt charge in response to changes in the load
19 forecast to maintain a level revenue. And we determine the charge
20 so that the billed amounts for each customer class apportion
21 responsibility for the cost of financing according to some proscribed
22 percentages. But that's the extent of the complication.

1 We usually distribute cash flows workbook (sans formulas) to the
2 rating agencies but have shared the model without modification
3 amongst client, bankers and financial advisors. We shared our model
4 with Guggenheim and Royal Bank of Canada during the last Duke
5 transaction. I also recall creating a custom worksheet for the client to
6 facilitate periodic true up calculations. All of this was pursuant to my
7 contract with no claim as to proprietary or trade secret.

8 **RATEPAYER-BACKED BONDS SHOULD NOT BE TREATED AS**
9 **ASSET-BACKED SECURITIES (ABS)**

10 **Q. IN ADDITION TO THE PROBLEMS IDENTIFIED ABOVE, WHAT**
11 **OTHER PROBLEMS HAVE YOU IDENTIFIED IN CONNECTION**
12 **WITH STRUCTURING AND MARKETING SECURITIZED UTILITY**
13 **RATEPAYER-BACKED BONDS?**

14 A. Any decisions to treat the proposed bonds as “asset-backed
15 securities” (ABS) when it should be treated as Ratepayer-Backed
16 Bond, as in the Duke Energy Florida Project Finance securitization
17 bond precedent in 2016, would likely reduce the potential savings to
18 ratepayers. The two structures are different in all material ways that
19 are of concern to investors. ABS are typically described with scenario
20 analyses that certainly include prepayment risk and might also
21 include risk of loss. Even AAA asset-backed securities with little or
22 no risk of loss trade at a wider spread than AAA corporates, at least
23 in part, because of variability in the timing of principal return.

1 Generally, AAA Ratepayer-Backed Bonds have no material risk of
2 loss and no material risk of timing variability because of the frequent
3 true up mechanism. This is because utilities' forecasts for demand
4 for a 6-12-month period are typically within a very modest variance
5 from actual demand which means cashflow is always very close to
6 what's expected. The strength and benefits of the true up mechanism
7 can't be emphasized enough. Commission financial advisors have
8 challenged underwriting firms' pricing utility securitization bonds
9 based on ABS credit spreads versus high-quality corporate credit
10 spreads as well as other issues that could affect pricing. They have
11 done so in an effort to negotiate credit spreads (and therefore the
12 cost to the ratepayer/customer) based on the power of the regulatory
13 true up mechanism of the charge on all customers on a joint basis
14 designed to ensure principal payment timing certainty and the legal
15 protections from the state not to interfere in the transaction.

16 From my 37 years of experience, I cannot emphasize enough this
17 fundamental difference: ABS begin with a fixed asset pool, and
18 investors will, generally, receive the cashflow from those assets
19 (protected from credit loss though a subordination of claims involving
20 a senior piece and a junior piece, but with no protection against
21 variations in the timing of principal payments) whenever the
22 payments happen to arrive. This represents a material prepayment
23 and extension risk. It means either investors receive their money

1 back sooner or later than expected, if at all. These risks and the
2 complexities associated with them are either not present or not
3 material in storm recovery bonds and other utility securitizations.

4 Storm recovery bonds, and other Ratepayer-Backed Bonds, begin
5 with a bond repayment schedule and have a true up mechanism to
6 ensure that's what investors will receive on time. It makes up for
7 losses or changes in demand by redistributing the charge on all
8 consumers in the utility's service territory on a joint basis. Paying
9 consumers make up for losses from non-paying consumers. That's
10 not a fixed pool of receivables like ABS. It's a charge on an essential
11 commodity, and if consumers leave the service territory, the charge
12 goes up on the customers that remain. If more consumers come into
13 the service territory, the charge goes down. All the Ratepayer-
14 Backed Bonds I have been involved with prohibit prepayment, and
15 the extension risk was not material.

16 In contrast, ABS investors who buy a pool of auto loans, credit cards,
17 or mortgages must look for repayment to a fixed pool. If one of the
18 payors in the pool defaults on their mortgage, auto loan, or credit
19 card, that loss is not redistributed to the mortgages, auto, loans and
20 credit cards of others in the pool. Those mortgages, auto loans or
21 credit cards are fixed. Their obligations don't go up to ensure the
22 bondholders are paid on time. But if that happens in a utility
23 securitization, the charges on those who are paying do go up. It's an

1 apples to oranges comparison when comparing ABS to utility
2 securitizations like the storm recovery bonds proposed by the
3 Companies.

4 **Q. IS THE FACT THAT RATINGS AGENCIES ASSIGN THE**
5 **TRANSACTIONS TO THEIR STRUCTURED FINANCE RATING**
6 **ANALYSTS MEAN THAT THEY ARE “ASSET-BACKED**
7 **SECURITIES” LIKE THOSE INCLUDED IN THE AGGREGATE**
8 **BOND INDEX THAT WITNESS ATKINS SAYS IS CRITICAL TO**
9 **STRUCTURING THE STORM RECOVERY BONDS?**

10 A. No. That they are handled in the Structured Finance group at the
11 rating agencies is sort of a historical accident. When the first
12 Ratepayer-Backed Bonds were contemplated, the corporate side of
13 rating agencies hadn't had experience with, for example, SPVs.
14 (special purpose vehicles or entities) So, even though there is no
15 asset credit risk or overcollateralization component to Ratepayer-
16 Backed Bonds, they landed in the structured finance group. That
17 needn't dictate how they are marketed or treated by underwriters and
18 investors.

19 **STRUCTURING DEC/DEP STORM RECOVERY BOND**
20 **ISSUANCES SO AS TO BE INCLUDED IN THE AGGREGATE**
21 **BOND INDEX AS ASSET BACKED SECURITIES (ABS) WILL**
22 **COST RATEPAYERS**

23 So, in my professional judgement, (i) it is very hard to justify that
24 Ratepayer-Backed Bonds like storm recovery bonds should be

1 marketed and priced as ABS for whatever reason including
2 attempting to include them in the Aggregate Bond Index as Witness
3 Atkins asserts, and (ii) treating them and suggesting in any way to
4 investors that they are asset-backed securities **would not be in the**
5 **ratepayers' best interest**, particularly given the objective to reduce
6 storm recovery charges to the maximum extent possible to achieve
7 the lowest cost and to create present value savings for ratepayers.

8 **SUCCESSFUL PRECEDENTS**

9 In addition, certain of the Ratepayer-Backed Bonds like the Duke
10 Energy Florida Project Finance bonds and the MP and PE
11 Environmental Funding bonds that I have modeled for utilities and
12 were successfully sold at tight credit spreads and have offered longer
13 weighted average life bonds than is available in the ABS market. The
14 ABS market is dominated by shorter maturities, generally 5-10 years
15 and the Companies' Ratepayer-Backed Bonds will have 15-20 year
16 maturities,

17 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

18 A. Yes.

1 Q. Mr. Heller, did you have a summary that you
2 would like to share with the Commission?

3 A. Yes, I do.

4 Q. Please proceed.

5 A. Okay. Thank you. I am owner of Analytic
6 Aid, a consulting company. I have approximately 25
7 years of investment banking experience at firms
8 including Merrill Lynch, Credit Suisse, and Bank of
9 America. My primary responsibilities were structuring
10 asset-backed securities, also known as ABS, such as
11 mortgage, residential and commercial, and non-mortgage,
12 student loan, pharmaceutical royalty, auto,
13 property-assessed clean energy, collateralized
14 financings, and developing models used in that
15 structuring. I have also structured seven issues of
16 Ratepayer-Backed Bonds, four while at an investment
17 bank and three as a consultant. I was a
18 structuring/financial modeler for the Duke Energy
19 Florida, approximately \$1.3 billion Ratepayer-Backed
20 Bond offering that received top ratings from Moody's,
21 S&P, and Fitch. It was also one of the longest
22 duration bonds ever structured at 20 years to scheduled
23 final maturity. I worked directly for Tom Heath of
24 Duke Energy and interacted with Saber Partners as the

1 financial advisor representing the ratepayers.

2 There are two items I want to highlight from
3 my testimony:

4 One, it does a disservice to Ratepayer-Backed
5 Bonds and the ratepayers who must pay their costs to
6 treat them as ABS. Ratepayer-Backed Bonds are
7 different from traditional ABS in all material ways
8 that are of concern to investors. ABS are typically
9 described with scenario analyses that certainly include
10 prepayment risk and might also include risk of loss.
11 Even AAA-rated ABS with little or no risk of loss trade
12 at a wider spread higher, you know, than AAA-rated
13 corporate securities like Johnson & Johnson and Exxon,
14 at least in part, because of the variability in the
15 timing of principal return. AAA-rated Ratepayer Backed
16 Bonds have no material risk of loss or payment
17 variability because of the frequent
18 legislatively-mandated and Commission-enforced true-up
19 mechanism. Investors can expect to receive the
20 scheduled cash flows with near perfect certainty.

21 Additionally, from my personal experience, I
22 have seen that ratepayers' interests are best served
23 when independent advisors are involved directly in
24 overseeing the structuring process. The lowest cost to

1 the ratepayer may not be the desired structure for the
2 underwriters. I worked, you know, at an investment
3 bank. We may have had prepared a preliminary structure
4 with a two-year weighted average life tranche of bonds,
5 and I would go to my bank's traders and say, you know,
6 "Here's a structure with a three-year weighted average
7 life tranche of bonds with all-in execution, that is,
8 for example, one basis point lower." They're very
9 likely to say something like, you know, "We already see
10 good appetite for the two-year weighted average life
11 tranche and one basis point is a rounding error," and I
12 might not disagree with them. But somewhere their
13 answer is gonna be the same at two or three basis
14 points, you know, or even more, and they might still
15 think we're at a rounding error, and an independent
16 advisor would be advocating for the lowest cost to the
17 ratepayer. On short maturities, a few basis points may
18 have limited impact with longer maturities to the
19 bonds, even one basis point can be significant and it's
20 likely -- you know, potentially can be, you know, a
21 couple basis points or more.

22 That's it.

23 MR. CREECH: Thank you, Mr. Heller. The
24 witness is available for cross examination.

1 CHAIR MITCHELL: All right. Ms. Athens,
2 the panel is available for cross examination.

3 CROSS EXAMINATION BY MS. ATHENS:

4 Q. Good morning, Mr. Sutherland and Mr. Heller.

5 A. (Steven Heller) Good morning.

6 Q. My questions today will be primarily to
7 Mr. Sutherland, and I just have a few short questions
8 on your testimony. If you could turn to page 11 of
9 your testimony, Mr. Sutherland.

10 So, on page 11, you answered the question
11 whether the Commission should give the Companies
12 flexibility to establish the terms and conditions of
13 the bonds; is that right?

14 CHAIR MITCHELL: Gentlemen, make sure
15 you are off mute when you are responding.

16 THE WITNESS: (Paul Sutherland) Yes,
17 I'm sorry. Yes, that is correct.

18 Q. And your answer to that question is no, the
19 Company should not be granted flexibility; is that
20 correct?

21 A. That's right. Not sole decision-making
22 flexibility, that's correct.

23 Q. And you go on to state that, "The exhibits I
24 am sponsoring," and I quote, "amply demonstrate the

1 benefits that accrued to ratepayers from providing the
2 Public Staff and its advisors equal authority with
3 other members of a bond team to make major decisions";
4 is that right?

5 A. That's correct.

6 Q. And what exhibits are you specifically
7 referring to in this statement?

8 A. I'm referring to the exhibits that
9 demonstrate interest rate savings on transactions that
10 have used best practices versus other transactions in
11 the same time frame. And specifically, that would be
12 Exhibit Number 2 regarding the Texas transactions
13 between 2001 and 2006. And Exhibit Number 7, which
14 demonstrates the Duke Energy Florida transaction in
15 2016. And also Exhibit Number 10, which demonstrates
16 interest rate savings in the Allegheny, West Virginia,
17 transaction in 2009.

18 Q. Thank you. So, in either of those three
19 exhibits, was a state consumer advocate or state
20 agency, other than the utilities Commission, a decision
21 maker?

22 A. I don't believe so, no. The decision maker,
23 the co-decision makers included Saber Partners as an
24 advisor to the Commission in a similar role to what

1 Saber Partners would be performing in this case with
2 the Public Staff.

3 Q. Thank you. So you would agree that your
4 exhibits only speak to transactions where the
5 Commission and either the public utility had
6 decision-making authority?

7 A. That is correct, because of the different
8 nature of those transactions' structure versus the way
9 the Public Staff operates in North Carolina, which is
10 somewhat different.

11 Q. And can you elaborate on those differences,
12 please.

13 A. Well, in the cases that I referred to, the
14 three cases, or the Texas case, the West Virginia case,
15 and the Florida case, the Commission had on staff a
16 representation that the main purpose and intent was
17 to -- for that staff to represent the ratepayers in a
18 situation such as this. And my understanding is that,
19 in North Carolina, the public service Commission, the
20 Utility Commission, does not directly represent the
21 ratepayer in a similar manner, but rather, relies on
22 Public Staff to perform that function.

23 Q. But were you here yesterday when you heard
24 the testimony of witnesses Rebecca Klein on behalf of

1 the Public Staff?

2 A. Yes, I was.

3 Q. And were you here when Chair Mitchell asked
4 her about who represented the ratepayers in Texas?

5 A. I believe I was.

6 Q. And Ms. Klein stated that Texas had another
7 state agency that represented their ratepayers and
8 small business customers; is that correct?

9 A. A segment of their ratepayers, yes.

10 Q. So again, you would agree that your exhibit
11 only speak to instances where the Commission or public
12 utilities had decision-making in those utility
13 securitizations?

14 A. That's correct.

15 Q. Thank you, Mr. Sutherland. That's all the
16 questions I have for you today.

17 And, Mr. Heller, I do not have any questions
18 for you.

19 MS. ATHENS: Chair Mitchell, thank you.

20 CHAIR MITCHELL: All right. Redirect
21 from the Public Staff?

22 MR. GRANTMYRE: The Public Staff does
23 not have redirect for Mr. Sutherland.

24 CHAIR MITCHELL: Okay. Questions from

1 the Commission beginning with

2 Commissioner Brown-Bland.

3 COMMISSIONER BROWN-BLAND: No questions.

4 CHAIR MITCHELL: All right.

5 Commissioner Gray?

6 COMMISSIONER GRAY: No questions.

7 CHAIR MITCHELL: Commissioner

8 Clodfelter?

9 COMMISSIONER CLODFELTER: I have
10 nothing.

11 CHAIR MITCHELL: Okay.

12 Commissioner Duffley?

13 COMMISSIONER DUFFLEY: No questions.

14 CHAIR MITCHELL: Commissioner Hughes?

15 COMMISSIONER HUGHES: No questions.

16 CHAIR MITCHELL: Okay.

17 Commissioner McKissick?

18 COMMISSIONER MCKISSICK: Two quick
19 questions, Madam Chair.

20 CHAIR MITCHELL: Yes, sir. Please
21 proceed.

22 EXAMINATION BY COMMISSIONER MCKISSICK:

23 Q. And this would be addressed to

24 Mr. Sutherland. Sir, I was just curious, since you --

1 I note that since Saber Partners has been serving as a
2 financial advisor to the Public Staff, and of course
3 your recommendation is that the Public Staff be an
4 official party to the bond team which would have equal
5 decision-making authority. Of course, Duke has
6 suggested that the Public Staff not be -- excuse me,
7 not be a part of that team formally and have
8 decision-making authority.

9 Do you think that you -- when I say you, I
10 should say Saber Partners, would be conflicted out in
11 the event the Commission had its own financial advisor,
12 independent of the Public Staff, to provide guidance to
13 the Commission?

14 A. (Paul Sutherland) If that financial advisor
15 to the Commission -- are you asking if that advisor to
16 the Commission were a Saber Partners or --

17 Q. That is correct.

18 A. -- another?

19 Q. No. The advisor to the Commission was Saber
20 Partners.

21 A. No, I don't think that would be a conflict at
22 all. In either case, we would be representing
23 ratepayer interest.

24 Q. Okay. And you spoke a lot about the

1 decisions that would be made by that bond team. And I
2 guess you envision that they would be involved with
3 selection of underwriters, perhaps involved in the
4 decision of attorneys that may be a part of this
5 process, establishing, you know, I guess, a marketing
6 plan for dealing with the bonds and things of that
7 sort.

8 When you have been involved in the past,
9 let's say down in Florida, did you address that full
10 range of issues, such as what is being proposed in this
11 case?

12 A. I think probably the analysts on the next
13 group from Saber Partners, like Mr. Fichera and the
14 like, can address that better than I, since my role is
15 primarily analytical and quantitative.

16 Q. I see. Very good. I don't have any further
17 questions at this time.

18 COMMISSIONER MCKISSICK: Thank you,
19 Madam Chair. Thank you, Mr. Sutherland.

20 THE WITNESS: Thank you.

21 CHAIR MITCHELL: All right. Thank you,
22 Commissioner McKissick. And I have nothing for the
23 witnesses, so I will see if counsel have questions
24 on Commissioner McKissick's questions.

1 MS. ATHENS: No questions for me.

2 CHAIR MITCHELL: All right.

3 Mr. Grantmyre?

4 MR. GRANTMYRE: Public Staff has no
5 questions.

6 CHAIR MITCHELL: All right. With that,
7 then, I will -- Ms. Cress, any from you?

8 MS. CRESS: CIGFUR has nothing. Thank
9 you, Chair Mitchell.

10 CHAIR MITCHELL: Okay. With that,
11 gentlemen, I believe you may step down.

12 Mr. Grantmyre, Mr. Creech --

13 MR. GRANTMYRE: Yes. I would move that
14 his testimony, if not already entered into
15 evidence, be entered into evidence, and his
16 Exhibits 1 through 11 -- I believe I said 1 through
17 10 earlier but there are actually 11 -- be entered
18 into evidence. Thank you.

19 CHAIR MITCHELL: All right. The 11
20 exhibits attached to Mr. Sutherland's direct
21 testimony will be admitted into evidence.

22 (Sutherland Exhibits 1 through 11, were
23 admitted into evidence.)

24 CHAIR MITCHELL: All right. With that,

1 gentlemen, you may step down.

2 MR. CREECH: Chair Mitchell, I'd also
3 like to move that Mr. Heller's testimony and
4 summary, and if I may, also Mr. Sutherland's
5 summary be entered into the record. I think we'll
6 also be filing those with the Commission.

7 CHAIR MITCHELL: All right. Hearing no
8 objection, Mr. Creech, your motion is allowed.

9 (Testimony was previously entered and
10 summaries were read into the record.)

11 CHAIR MITCHELL: All right. Gentlemen,
12 you may step down. Thank you very much for your
13 time this morning.

14 THE WITNESS: (Steven Heller) Thank
15 you.

16 THE WITNESS: (Paul Sutherland) Thank
17 you.

18 CHAIR MITCHELL: All right.
19 Mr. Grantmyre, Mr. Creech, you all may call your
20 next witnesses.

21 MR. CREECH: Chair Mitchell, we are
22 calling our finance panel, which is going to be
23 comprised of Joseph Fichera, Brian Maher,
24 Hyman Schoenblum, and Bill Moore.

1 CHAIR MITCHELL: All right. Gentlemen,
2 I let me identify you on my screen. Mr. Maher, I
3 need you to turn your camera on. Mr. Moore, let's
4 see. All right. Mr. Moore, I'm not seeing you.
5 Oh, there you are.

6 Whereupon,

7 JOSEPH FICHERA, BRIAN A. MAHER, HYMAN SCHOENBLUM,
8 AND WILLIAM MOORE,

9 having first been duly affirmed, were examined
10 and testified as follows:

11 CHAIR MITCHELL: All right. Thank you
12 very much. And gentlemen, I'm getting some
13 feedback, so I would ask that each of you mute
14 yourself unless you are going through the opening
15 statements with your attorney. So please remain
16 muted until it's your turn to speak. All right.
17 You may proceed, Mr. Grantmyre and Mr. Creech.

18 MR. GRANTMYRE: Chair Mitchell, I just
19 want to give you the order of witnesses. It will
20 be Mr. Fichera, then Mr. Maher, then
21 Mr. Schoenblum, and then Mr. Moore. And Mr. Creech
22 will be sponsoring Mr. Fichera and Schoenblum, and
23 I will be sponsoring Mr. Maher and Mr. Moore. So
24 Mr. Fichera is first.

1 DIRECT EXAMINATION BY MR. CREECH:

2 Q. Good morning, Mr. Fichera.

3 A. (Joseph Fichera) Good morning.

4 Q. Please state your name and address for the
5 record.

6 A. Name is Joseph S. Fichera. My business
7 address is 260 Madison Avenue, Suite 8019, New York,
8 New York.

9 Q. And you're testifying today on behalf of the
10 Public Staff; is that correct?

11 A. Yes, I am, sir.

12 Q. And did you cause to be filed in these
13 dockets on December 21, 2020, direct testimony
14 consisting of 68 pages and six exhibits, and
15 corrections filed on January 6, 2021, and revised
16 corrections and fully memorialized testimony on
17 January 13, 2021, of course with those six exhibits
18 having been filed originally on December 21, 2020?

19 A. Yes, that is correct.

20 Q. Do you have any corrections to your
21 testimony?

22 A. No, I don't.

23 Q. If you were asked the same questions today,
24 would your answers be the same?

1 A. Absolutely, yes, they would.

2 MR. CREECH: Chair Mitchell, at this
3 time I'd move that Mr. Fichera's prefilled direct
4 testimony and exhibits be copied into the record as
5 if given orally from the stand -- excuse me.

6 Prefilled direct testimony be copied into the record
7 as if given orally from the stand and that his six
8 exhibits be marked for identification as premarked
9 in the file.

10 CHAIR MITCHELL: All right. Mr. Creech,
11 hearing no objection to your motion, it is allowed.

12 (Fichera Exhibits 1 through 6, were
13 identified as they were marked when
14 prefilled.)

15 (Whereupon, the prefilled corrected
16 direct testimony of Joseph Fichera was
17 copied into the record as if given
18 orally from the stand.)

19
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24

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

DOCKET NO. E-2, SUB 1262

DOCKET NO. E-7, SUB 1243

In the Matter of

Joint Petition of Duke Energy)
 Carolinas, LLC and Duke Energy)
 Progress, LLC Issuance of Storm)
 Recovery Financing Orders)
)
)

DIRECT TESTIMONY OF
 JOSEPH S. FICHERA CHIEF
 EXECUTIVE OFFICER OF
 SABER PARTNERS, LLC

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

Docket No. E-2, Sub 1262

Docket No. E-7, Sub 1243

Direct Testimony of

Joseph S. Fichera

Senior Managing Director and Chief Executive Officer

Saber Partners, LLC

December 21, 2020

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INTRODUCTION

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. Joseph S. Fichera, Saber Partners, LLC, 260 Madison, Suite 8019
3 New York, New York 10016.

4 **Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR
5 POSITION?**

6 A. I am a member of Saber Partners, LLC and serve as its Chief
7 Executive Officer.

8 **Q. PLEASE BRIEFLY DESCRIBE YOUR DUTIES AND
9 RESPONSIBILITIES IN THAT POSITION.**

10 A. I manage the organization and execute assignments for clients by
11 providing confidential, independent, senior-level analysis, advice, and
12 execution for chief executive officers, regulators, elected officials, chief
13 financial officers, treasurers and others. Since 2001, our firm has focused
14 on achieving lowest cost for ratepayers in Ratepayer-Back Bond
15 transactions.

16 **Q. WHAT IS YOUR EDUCATIONAL BACKGROUND AND
17 PROFESSIONAL EXPERIENCE?**

18 A. I have a Bachelor's degree in Public Affairs from Princeton
19 University's Woodrow Wilson School of Public and International Affairs. I
20 also have a Master's degree in Business Administration from Yale

1 University's School of Management. In 1995-1996, I was an executive
2 fellow in residence at the Woodrow Wilson School of Public and
3 International Affairs at Princeton. In 2018 the National Regulatory Research
4 Institute (NRRI) part of the National Association of Regulatory Utility
5 Commissions (NARUC) selected me to be one their first ever "National
6 Fellows" for 2018-2019. In connection with that, I wrote an article for the
7 NRRI on securitization transactions for investor-owned electric utilities/
8 Ratepayer-Backed Bonds that was published in January 2019. The
9 economic burden of repaying these bonds falls squarely on the ratepayers
10 in the service territory; hence they are aptly referred to as "Ratepayer-
11 Backed" bonds (Ratepayer-Backed Bonds).

12 Since 1982, I have worked in the fields of finance and investment banking.
13 I began as an Associate in the Public Finance Department of Dean Witter
14 Reynolds (now a part of Morgan Stanley) from 1982-1984. I then served as
15 Vice President in Corporate Finance at Smith Barney Harris Upham (now a
16 part of Citigroup) from 1984-1989. I became a Managing Director, Principal
17 in Corporate Finance and Capital Markets at Bear Stearns and Co, Inc. from
18 1989-1995. Following my fellowship at Princeton in 1996, I served as
19 Managing Director and Group Head of Prudential Securities Business
20 Origination and Product Development Unit from 1997-2000. With several
21 colleagues from the utility, law, and banking industries, I formed Saber
22 Partners, LLC in 2000. I have held a general securities principal license

1 (Series 24) from the U.S. Securities and Exchange Commission (SEC) as
2 well as a general securities representative license (Series 7 and 63).
3 Since forming Saber Partners, I have engaged in many complex
4 assignments in the energy and finance field. I served as a chief financial
5 advisor, along with the Blackstone Group, to the governor of the State of
6 California during 2001. We assisted in developing the Governor's response
7 to the energy crisis beginning in March 2001. I also have served as the
8 chief financial advisor to six state utility commissions or their agents
9 (Florida, Texas, West Virginia, Wisconsin, Vermont, and New Jersey) and
10 the Office of the People's Counsel for the District of Columbia on the use of
11 Ratepayer-Backed Bonds and specifically the structuring, marketing, and
12 pricing of approximately \$9.25 billion in Ratepayer-Backed Bonds. I have
13 also been engaged as an advisor to the SEC and ExxonMobil Corporation,
14 among others. I currently serve on the Board of Advisors of Princeton's
15 Center for Economic Policy Studies. I also served as Chairman of the
16 Princeton Economics Department Advisor Council. In that capacity, I
17 served as an advisor to Federal Reserve Chairman Ben Bernanke when he
18 was the Chairman of the Economics Department of Princeton University in
19 the 1990s. My vitae is attached to this testimony as Fichera Exhibit 1.

1 **Q. DURING YOUR CAREER ON WALL STREET, DID YOU**
2 **PARTICIPATE IN ANY UNDERWRITINGS – THE SALE OF SECURITIES**
3 **TO INVESTORS IN PUBLIC OFFERINGS?**

4 A. Yes. The primary focus of my positions from Associate to Managing
5 Director was first to advise on, structure, and execute on underwritings and
6 private placements of debt and equity issuances. My role evolved to
7 providing strategic advice to corporate treasurers, chief financial officers,
8 and chief executive officers.
9 My responsibilities included advising all these officers and their legal
10 counsel on the structuring, marketing, and pricing of publicly-offered
11 securities. I also led or participated in corporate reorganizations and
12 restructurings. My underwriting experience included direct negotiations
13 with corporations, utilities, and investors over the structuring, marketing and
14 pricing of publicly-offered debt and equity securities. My primary role was
15 as the Bookrunning Underwriter, sole manager or senior manager. I also
16 have experience as a co-managing Underwriter of publicly-offered debt and
17 equity securities.¹

¹ As an Underwriter, I received three “Deal of the Year” awards from industry publications. These are awards for transactions that independent observers who closely follow the profession consider significant and merit the attention of one’s peers. In 1990, for a preferred stock transaction, I received the award from “Institutional Investor” magazine. In 1991, I received this award again for an investor-owned utility debt reorganization in the municipal bond market. In 2003, I was recognized with a similar “Deal of the Year” award from “Asset Securitization Report” for a Ratepayer-Backed Bonds offering. “Deal of the Year” awards generally identify transactions that have unique features, overcame specific market obstacles or set precedents in the financial markets.

1 **Q. HAVE YOU PARTICIPATED IN TRANSACTIONS INVOLVING**
2 **RATEPAYER-BACKED BONDS SIMILAR TO THE STORM RECOVERY**
3 **BONDS PROPOSED BY THE JOINT PETITION?**

4 A. Yes. To-date, I have participated in 13 Ratepayer-Backed Bond
5 transactions for over \$9.25 billion, involving eight different investor-owned
6 electric utilities.

7 **Q. HAVE YOU HAD DIRECT INTERACTIONS WITH INVESTORS,**
8 **UNDERWRITERS AND REGULATORS CONCERNING THE TYPE**
9 **OF SECURITIES THAT ARE THE SUBJECT OF THE JOINT PETITION?**

10 A. Yes.

11 **Q WAS YOUR INTERACTION WITH BOTH UNDERWRITERS AND**
12 **INVESTORS?**

13 A. Yes, with many investors, underwriters, counsel and others in my
14 capacity as the financial advisor on an ongoing basis over the past 20 years.

15 **Q. HOW DID YOU INTERACT WITH INVESTORS? ISN'T THAT**
16 **SOLELY THE JOB OF THE UTILITY AND THE UNDERWRITERS?**

17 A. Ratepayer-Backed-Bond issues are unique because they are a
18 direct borrowing on the credit of all the utility's ratepayers supported by a
19 unique guarantee of the regulator. The special characteristics of the
20 authorizing legislation and the financing order (Financing Order) often raise
21 many questions about the financing order. As the regulator's financial

1 advisor and from the perspective of the regulator and ratepayers, I have
2 explained the commission's important role in writing the terms of the
3 Financing Order. The Financing Order is the basis for the bond financing
4 and implementing the adjustment mechanism known as the true-up
5 mechanism. I have assisted staff and others in discussing the Financing
6 Order, the authorizing legislation, and the support for the financing. This
7 included discussing the benefits of the transaction for the ratepayer and
8 regulator as well as the relative value of this credit mechanism to other
9 mechanisms in the marketplace.

10 **Q. WERE THESE INDIVIDUAL MEETINGS OR GROUP**
11 **PRESENTATIONS?**

12 A. Both. I have spoken directly with individual investors and
13 Underwriters as well as participated in what are known as investor
14 roadshows, both electronically and in person, on each offering of
15 Ratepayer-Backed Bond offerings.

16 I have also conducted various "teach-ins" with Underwriters and their
17 salesforces. There often is a great deal of incorrect information,
18 misinformation and just plain myths about Ratepayer-Backed Bonds.
19 Providing accurate information about the particular Ratepayer-Backed
20 Bonds being offered, as well as the particular Financing Order, to market
21 participants is an important function at Saber Partners.

1 Q. HAVE YOU SPOKEN AT MEETINGS OF THE NATIONAL
2 ASSOCIATION OF REGULATORY COMMISSIONERS (NARUC) OR OF
3 OTHER UTILITY ASSOCIATIONS AND CONSUMER GROUPS, AND
4 INVESTOR FINANCIAL CONFERENCES ON MATTERS RELATED TO
5 THE ISSUES IN THE JOINT PETITION?

6 A. Yes. A core part of my job at Saber Partners has been as a resource
7 to regulatory commissioners and their staffs, consumer groups, investors
8 and others interested this type of financing. In 2006, 2009 and 2018,
9 NARUC asked me in to present at their meeting on utility securitization
10 issues. In addition, the NARUC Subcommittee on Electricity asked me to
11 present to the Subcommittee alongside Jon McKinney, former Chairman of
12 the West Virginia Public Service Commission (WVPSC), at the May 2019
13 monthly meeting.

14 The Society of Utility Regulatory and Research Financial Analysts (SURFA)
15 asked me to address Ratepayer-Backed Bonds at their annual meeting in
16 April 2019. In addition, they requested that I help organize and participate
17 in a July 2020 webinar on utility securitization/Ratepayer-Backed Bonds as
18 a possible tool to address costs arising from the COVID-19 pandemic.

19 The National Association of State Utility Consumer Advocates (NASUCA)
20 asked me to address their Accounting Committee in July 2020 and to
21 organize a panel and speak at their national annual meeting on November
22 9, 2020 concerning the Ratepayer-Backed Bond financing tool and the

1 issues concerning protecting consumers. NASUCA had previously asked to
2 address their national annual meeting in 2009.

3 The Investor Management Network (IMN) asked me to lead panel
4 discussions on issues related to Ratepayer-Backed Bonds in 2003 and
5 2005 at their conference of 3,000 or more participants known as “ABS East.”

6 I also was asked to lead a panel discussion on pricing transparency – the
7 ability for investors and regulators to see actual trades for prices of
8 securities transactions – in 2007 and 2008. The 2007 panel led to major
9 reforms of the entire securitization market in 2011.

10 **TESTIMONY FROM OTHER SABER PARTNER WITNESSES**

11 **Q. WHO ELSE FROM SABER PARTNERS WILL BE PROVIDING**
12 **TESTIMONY?**

13 A. Testimony concerning the Joint Petition will be submitted by:

14 **Rebecca Klein**, former Chair of the Public Utility Commission of Texas
15 (PUCT) and a member of the Saber Partners Advisory Board since 2006;

16 **Hyman Schoenblum**, former Treasurer and a top Financial Officer during
17 a 30-year career at Consolidated Edison Company of New York and a
18 Senior Advisor to Saber Partners;

19 **Barry Abramson**, former utility equity analyst and investment advisor and
20 a Senior Advisor to Saber Partners;

1 **Brian A. Maher**, former Assistant Treasurer and 30-year veteran of Exxon
2 Mobil Corporation for external finance and a Senior Advisor to Saber
3 Partners;

4 **Paul Sutherland**, former Assistant Treasurer of Florida Power and Light
5 Company and a Senior Advisor to Saber Partners;

6 **Steven Heller**, President of Analytical Aid who has been an independent
7 modeler of Ratepayer-Backed Bonds and is a consultant to Saber Partners
8 for the purpose of evaluating certain aspects of the Joint Petition; and

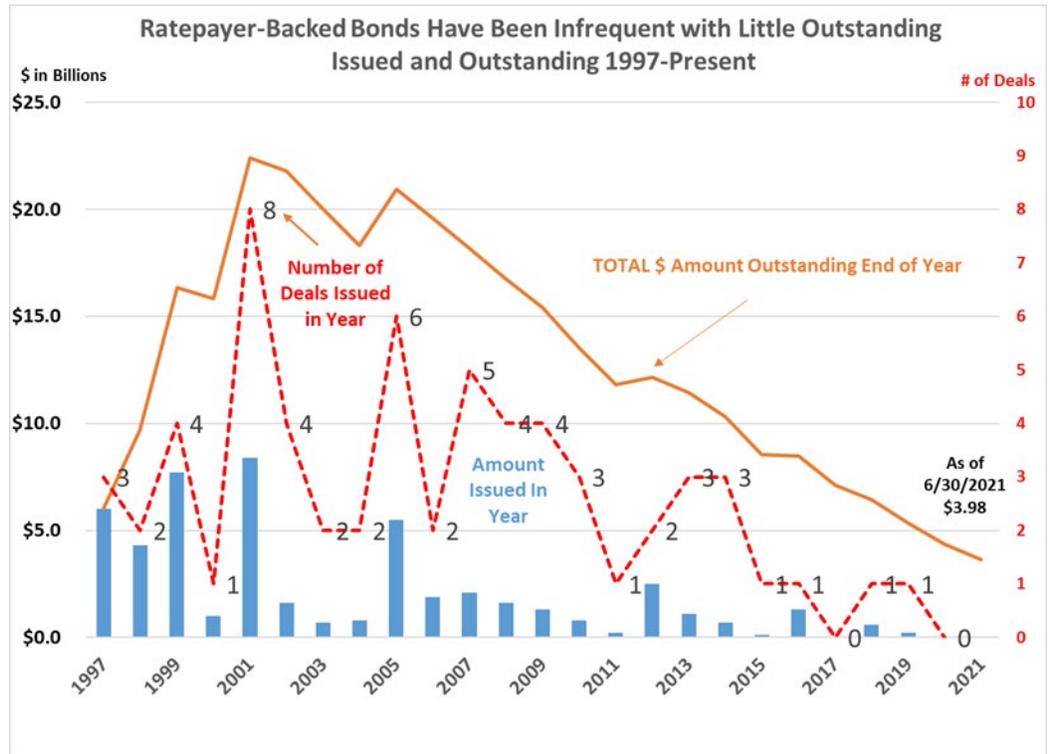
9 **William B. Moore**, whose career began as a financial assistant in the
10 treasury department of Kansas Gas & Electric and rose to Chief Financial
11 Officer and then Chief Executive Officer of Westar Energy. He was one of
12 the founding partners of Saber Partners in 2000 before returning to Westar
13 to become President and then CEO with the financial function reporting to
14 him.

15 Because of the technical nature of the issues that are generally not
16 discussed in regulatory proceedings, I am attaching a Glossary of terms as
17 Fichera Exhibit 6, for reference in my testimony and the testimony of other
18 Public Staff witnesses. Except as otherwise defined in my testimony,
19 capitalized terms have the meanings assigned to them in the Glossary.

1 HISTORICAL ISSUANCES OF RATEPAYER-BACKED BONDS
 2 CREATE CHALLENGES

3 Q. BECAUSE THIS IS THE FIRST TIME THE COMMISSION IS
 4 ADDRESSING THESE ISSUES, WHAT SHOULD THEY KNOW ABOUT
 5 THE MARKET FOR RATEPAYER-BACKED BONDS

6 *Fichera Figure 1*



7

8 There are critical marketing issues to consider when establishing North
 9 Carolina’s Storm Recovery Bond program. It is true that Ratepayer-Backed
 10 Bonds have been around for about 20 years, and as the Companies’
 11 witness Atkins has noted, approximately \$50 billion have been issued in 65
 12 different transactions for investor-owned utilities. However, these bond
 13 issuances have been infrequent, and there are very few bonds remaining

1 outstanding in investor hands when the Companies expect to come to
 2 market. The chart above shows the amount issued and outstanding over
 3 this 23 year timeframe. This is small when compared with the amount of
 4 corporate, utility, and structured finance debt in the market. As a result, a
 5 very large part of the market is not familiar with the financing mechanism.
 6 The good news is that while Ratepayer-Backed Bonds are relatively small
 7 and infrequent, they are the only asset sector that has never experienced a
 8 downgrade nor even been on a watchlist for a downgrade by any rating
 9 agency.

10 **THREE PHASES OF THE CURRENT RATEPAYER-BACKED BOND**
 11 **PROCESS**

12 **Q. ARE THERE ANY DISTINCT PHASES OF ISSUING RATEPAYER-**
 13 **BACKED BONDS OF WHICH THE COMMISSION SHOULD BE AWARE?**

14 Following the enactment of enabling legislation, there are three distinct
 15 phases for a Ratepayer-Backed Bond sale that the Commission should
 16 consider and in which it should be actively engaged.

17

Fichera Figure 2



1
**Petition for
 Financing
 Order; Write
 Detailed
 Financing
 Order**



2
**Implementation
 of the Financing
 Order**



3
**Price Bonds
 Through Sale to
 Investors**

18

1 **Phase One: The Petition for a Financing Order and Writing of the**
2 **Detailed Financing Order.**

3 The Financing Order should be carefully written because it is the basis for
4 the credit associated with the bonds. As the Companies' witnesses Heath
5 and Atkins correctly point out, the precise bond structure, interest rates and
6 other costs cannot be known with certainty at the time the Financing Order
7 is issued. For this reason, the Companies have requested "flexibility"
8 following the issuance of the Financing Order to determine the final
9 structure including the interest rate during the subsequent two phases of
10 the process.

11 **Phase Two: Implementation of the Financing Order.**

12 This is the time between the issuance of the Financing Order and the
13 issuance of the bonds at which time the Financing Order becomes final and
14 irrevocable. This phase involves multiple other parties, including nationally
15 recognized bond rating agencies, to consider the structure of the bonds,
16 their maturity and ability to pay principal and interest. It also involves
17 regulatory, tax, bankruptcy, state and federal law counsel. This phase also
18 includes material decisions regarding the method of sale.

*Fichera Figure 3***Phase 2 Activities Affecting Ratepayers Include:**

- Rating agency discussions, financial modeling stress testing, negotiations
- Documentation of transaction components and legal opinions
- Offering materials including prospectus
- Securities and Exchange Commission filings and discussions
- Selection of offering method – competitive bid or negotiated transaction
- Selection of underwriters
- Requesting, analyzing and oversight of marketing plan and plan of distribution
- Teach-ins for underwriters; investor presentations

1
2 During this second phase, there is extensive modeling of cashflows that will
3 support the bond based on the examination of the utility's historical
4 forecasts and collections as well as its projections over the next 20 years.
5 This is done to achieve a top credit rating on the bonds from nationally
6 recognized rating agencies like S&P and Moody's for the possibility of
7 achieving the lowest interest rates from investors.
8 Offering documents are developed and submitted to the Securities and
9 Exchange Commission.
10 The method of sale is decided (competitive bid or negotiated transaction)
11 and a marketing plan is developed.
12 **Phase Three: Pricing the Bonds and Sale to Investors.**
13 Depending on the method of sale chosen, this is the process that concludes
14 the marketing process and establishes the final interest rate in relation to
15 the interest rates on benchmark securities used for comparison for a chosen

1 maturity and principal repayment schedule. Witness Sutherland describes
 2 this process in detail in his testimony. This is a dynamic process.

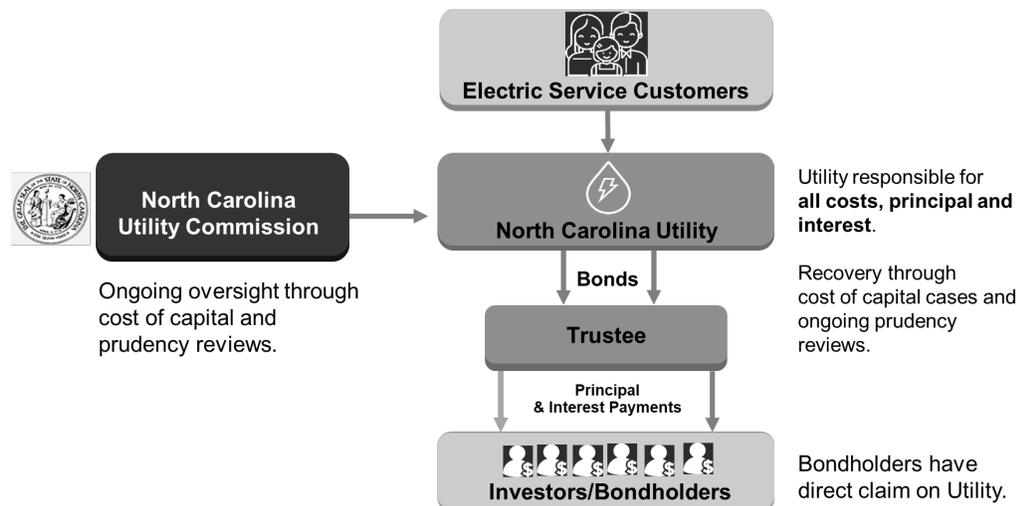
3 **COMPARISON BETWEEN TRADITIONAL UTILITY BONDS AND**
 4 **RATEPAYER-BACKED BONDS**

5 **Q. HOW ARE TRADITIONAL UTILITY BONDS STRUCTURED?**

6 Traditional utility bonds are simple and straightforward. The structure,
 7 marketing, and pricing are streamlined because the utility is a frequent
 8 issuer, i.e., often in the market with a great deal of information readily
 9 available to investors. Offering documents often have been prepared in
 10 advance and are on file with the Securities and Exchange Commission.

11 As can be seen by the chart below, the structure of a traditional utility bond
 12 is direct debt of the utility with the commission retaining all regulatory
 13 authority over the utility and all customer rates.

14 *Fichera Figure 4*



15
 16 Traditional bonds are direct debt/obligations of the utility. Bondholders only
 17 have a claim on the utility and its assets such as its plant and equipment.

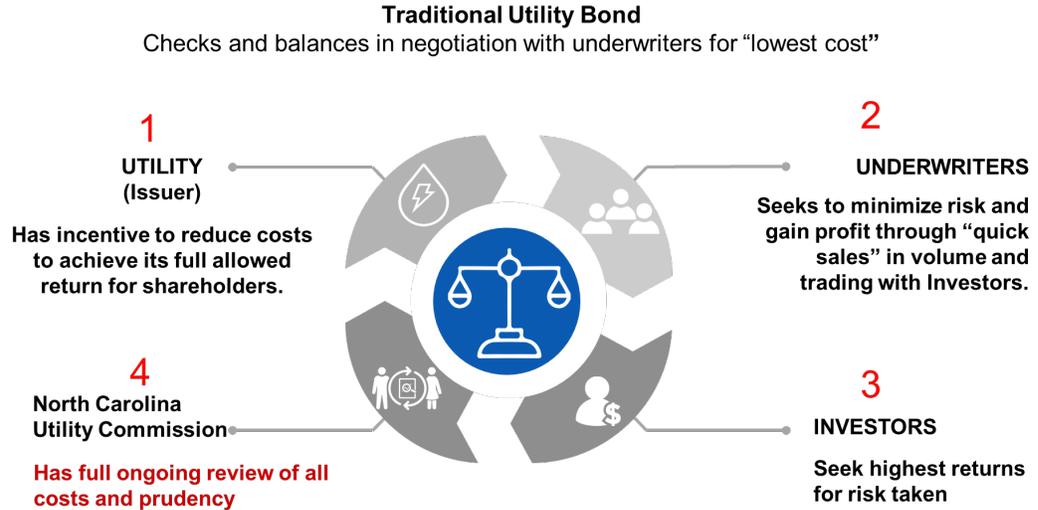
1 In fact, the utility has different levels of security for its debt, like first
2 mortgage bonds that are secured, and other bond issues that are not
3 secured by any claim on property. There is no direct claim on the ratepayers
4 or any specific component of customer rates.

5 From the perspective of the bondholder, the revenue requirements from
6 customer rates to pay principal and interest on traditional utility bonds are
7 not certain. The utility only gets revenues from customer rates approved by
8 the commission through cost of capital proceedings. Those revenues go to
9 all utility costs, including costs of operations, maintenance, taxes, and
10 returns for shareholders, not just principal and interest on bonds.

11 **Q. ARE THERE CHECKS AND BALANCES IN THE STRUCTURING,**
12 **MARKETING AND PRICING OF TRADITIONAL UTILITY BONDS?**

13 A. Yes. As more fully explained by Public Staff witness Schoenblum, there
14 are built-in “checks and balances” because the Commission retains full
15 regulatory review of the utility’s costs and the Utility can achieve its allowed
16 returns for shareholders to whom they have a fiduciary duty.

1 *Fichera Figure 5*

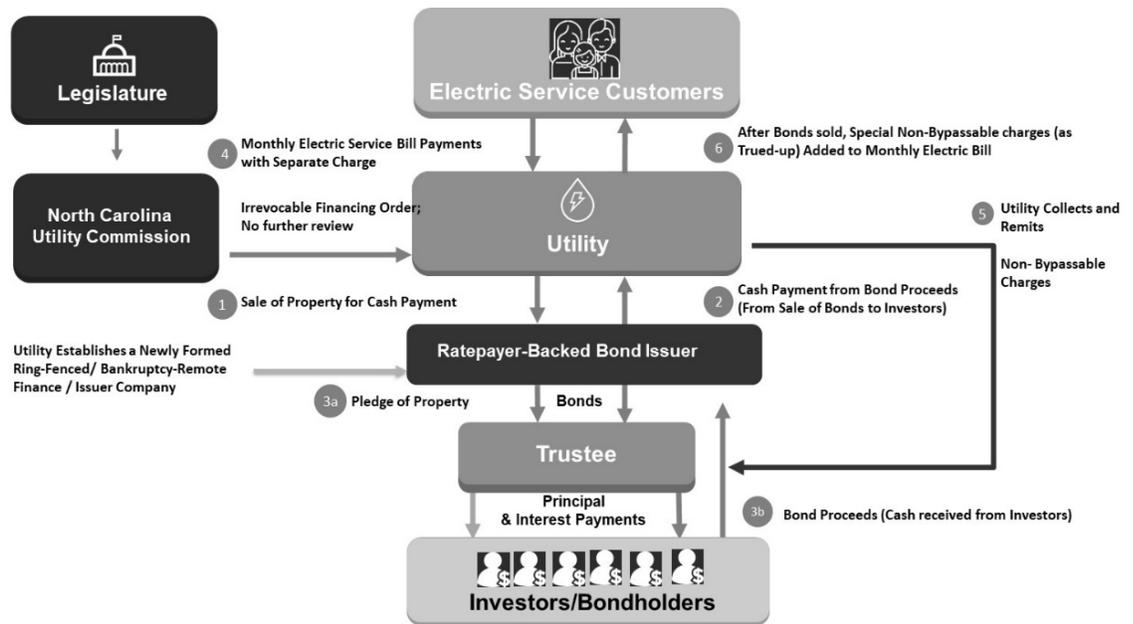


2 When a utility decides to issue a traditional bond, the utility has a strong
 3 incentive to negotiate hard with underwriters for the lowest possible interest
 4 rates as well as the lowest possible underwriting fees. Utilities also have a
 5 strong incentive to minimize other issuance costs. These same incentives
 6 do not come into play in connection with Ratepayer-Backed Bonds.
 7 In each case, underwriters act as middlemen between the utility issuing the
 8 bonds and the investors. Investors seeking bonds look for the highest
 9 return, and they weigh the lending rate against the risk. Through – and after
 10 – the process, the Commission retains its regulatory review authority over
 11 the utility’s cost of capital and may disallow any costs that it considers not
 12 prudent, just or reasonable.

1 **Q. HOW IS A RATEPAYER-BACKED-BOND DIFFERENT?**

2 A. As illustrated by the chart below, the structure of the bond is
 3 materially different, more complex than a traditional utility bond. The
 4 bondholder is a creditor of a special issuer but with a dedicated and specific
 5 charge on all ratepayers. None of the utility’s creditors have a claim on
 6 those revenues even in a bankruptcy. The utility, after receiving the
 7 proceeds of the bond sale, in this case is merely acting as the “servicer” of
 8 the Ratepayer-Backed Bonds. This means they simply calculate, charge,
 9 bill and collect the revenue from ratepayers to repay the bonds on time.

10 *Fichera Figure 6*

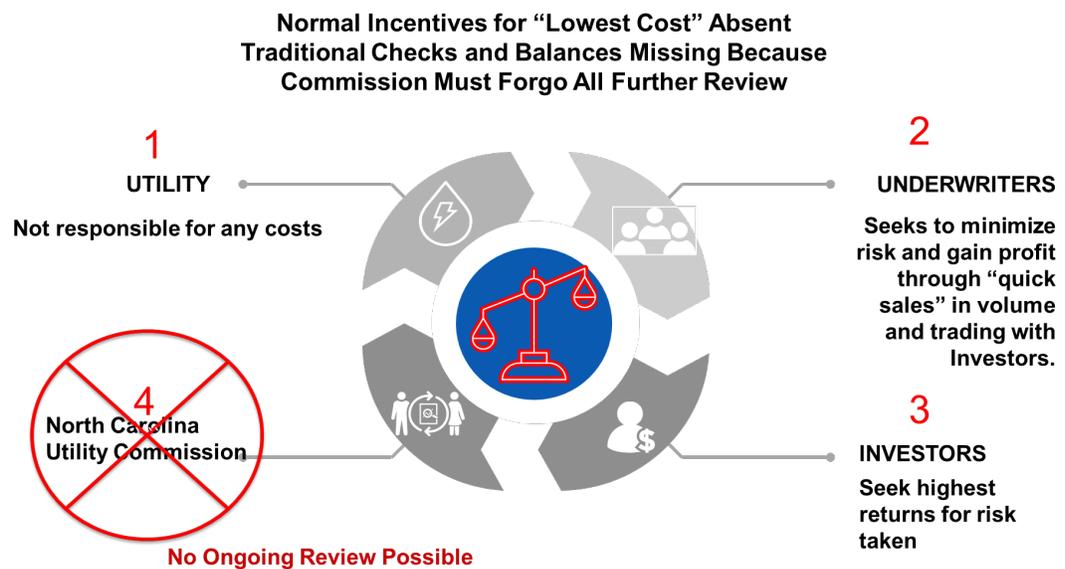


11

1 **Q. ARE THERE THE SAME FINANCIAL INCENTIVES FOR THE**
 2 **UTILITY PRESENT IN A RATEPAYER-BACKED BOND THAT ARE**
 3 **PRESENT IN A TRADITIONAL BOND?**

4 A. No. The issuer of Ratepayer-Backed Bonds is a new entity
 5 established for the sole purpose of selling the Ratepayer-Backed Bonds,
 6 not the utility. The only collateral this new issuer has to pledge to investors
 7 is the storm recovery property created by the statute and the Financing
 8 Order that contains the True-Up Mechanism and the state pledge of non-
 9 interference in the rights of the bondholders to be repaid on time.

10 *Fichera Figure 7*



11
 12 The testimonies of Public Staff witnesses Hyman, Schoenblum, and Klein
 13 explain in more detail why the interests of ratepayers and the sponsoring
 14 utility might not be aligned in the underwriting of Ratepayer-Backed Bonds.
 15 While the utility has a general business interest in keeping overall customer
 16 rates low, it will have no direct or indirect obligation to repay the Ratepayer-

1 Backed Bonds and will have no direct or indirect responsibility to pay any of
2 the financing costs. The ratepayers alone will bear all costs. Therefore, the
3 sponsoring utility may have no economic incentive to achieve the lowest
4 possible cost and the lowest possible storm recovery charges, although it
5 may have other incentives, such as a corporate policy, to achieve the
6 “lowest costs.”

7 That said, the sponsoring utility’s highest priority will likely be to get the
8 issuance done quickly, and cost may take a lower priority.

9 **Q. WOULD GRANTING THE COMPANIES “FLEXIBILITY” IN THE**
10 **FINANCING ORDER SOLVE THE PROBLEM?**

11 A. It solves one problem and creates another. With flexibility, the
12 outcome that the Commission expects at the time it issues the Financing
13 Order could change dramatically and materially for reasons both within and
14 beyond the control of the Companies. The Companies recognize this and
15 have proposed an Issuance Advice Letter process in Phases Two and
16 Three where only one Designated Commissioner would be involved - at a
17 very high level - during the Phase Two process following the issuance of
18 the Financing Order as the bonds are structured, marketed and priced. This
19 is when many material decisions are made and the storm recovery charges
20 and the Commission are locked in. The Companies would file an “Issuance
21 Advice Letter” at the end of Phase Three and propose that the full
22 Commission would be given the opportunity to disapprove the bond offering.

1 However, this would be after the Companies made all the decisions as to
2 the structure, marketing and pricing of the bonds. They would provide
3 “timely information” to the Commissioner and staff upon request.

4 **Q. ISN'T THAT SUFFICIENT?**

5 A. No. We agree that the Commission should make the final “go, no
6 go” decision. And we agree that there should be an Issuance Advice Letter
7 filed. But the process leading up to that final decision needs to produce an
8 informed and meaningful evidentiary record for the Commission to review
9 and consider. The Companies’ proposal excludes the representative of the
10 ratepayers, the Public Staff, from this important phase of the ratemaking
11 process. Moreover, it does not provide the Commission with independent
12 information and the analysis of technical information upon which to make
13 an informed decision. As explained by other Public Staff witnesses
14 Schoenblum, Klein, Sutherland, Maher and Abramson, the complexity of
15 the Ratepayer-Backed Bond structure, marketing and pricing process
16 requires the consideration and evaluation of specific and highly technical
17 information. It requires a robust process of due diligence so that the
18 Commission has a fully vetted evidentiary basis on which to make that final
19 “go, no go” decision. Anything less is insufficient.

20 For the Commission to make an independent “go, no go” decision, it needs
21 expert analysis of the information it receives. Simply being “informed” of
22 the decisions being made by the Companies, who have a direct financial

1 interest in the outcome that is different from the ratepayers, has been found
2 by many other state utility commissions to be an insufficient basis for
3 fulfilling their responsibilities to ratepayers.

4 It should be noted that capital market participants often have differing views
5 on the same information. That's what a market is by definition.

6 One caveat, however, is important. Parties who have a direct financial or
7 economic interest in the outcome may view certain information differently
8 from those who do not. If there were not differing and competing views
9 about the same information, there would not have been the significant
10 difference in investor orders for Ratepayer-Backed Bonds at proposed
11 yields that we have seen. So, the phrase "Trust but verify" applies.

12 **PRECEDENTS FROM OTHER STATES TO CONSIDER**

13 **Q. WHAT HAVE OTHER STATES DONE THAT THE COMMISSION** 14 **SHOULD CONSIDER?**

15 A. Over the past 20 years, certain "best practices" have emerged and
16 are discussed in more detail by Public Staff witnesses Klein, Schoenblum,
17 Sutherland and Heller. The first "best practice" is for the commission to
18 create a post Financing Order and pre-bond issuance review process. In
19 this process, the many technical and market-related issues raised in the
20 Joint Petition and by Public Staff in this testimony can be thoughtfully
21 considered and discussed by all parties affected by the transaction.
22 Following these proven "best practices" means amending the Companies'

1 proposal for “flexibility” to ensure that ratepayers are at the negotiating
2 table. Many years of experience have shown that it is essential that
3 ratepayers be on equal footing with the Companies, the underwriters and
4 the investors as post-Financing Order decisions are made about the final
5 structuring, marketing and pricing of the bonds. Every dollar in this
6 transaction is a ratepayer dollar. Being outside the negotiation room and
7 then being told “that’s the best we could do” is vastly different than being in
8 the room, at the table.

9 **Q. DOES N.C. GEN. STAT. § 62-172 AUTHORIZE THE NCUC TO**
10 **INCLUDE PROVISIONS IN A FINANCING ORDER THAT ARE**
11 **DESIGNED TO ENSURE THE LOWEST COST OF FUNDS AND OTHER**
12 **RATEPAYER PROTECTIONS?**

13 A. Yes. N.C.G.S. § 62-172(b)(3)b.12. directs the Commission to
14 include “any other conditions that the commission considers appropriate
15 and that are not otherwise inconsistent with this section.” This not only
16 authorizes, but directs the NCUC to impose conditions that are designed to
17 ensure the lowest possible storm-recovery charges and the greatest
18 possible ratepayer protections.

1 **Q. ARE ALL THE ELEMENTS FOR A SUCCESSFUL RATEPAYER-**
2 **BACKED BOND TRANSACTION PRESENT IN THE JOINT PETITION?**

3 A. No. There are both substantive and procedural deficiencies in the
4 Companies' Joint Petition that do not follow best practices. These
5 deficiencies are addressed in the testimony of Public Staff witnesses Klein
6 and Schoenblum and also later in my testimony. These deficiencies should
7 be addressed early so that the Commission, Public Staff and the
8 Companies can work in a cooperative manner to complete the transaction
9 expeditiously.

10 **COMMISSION AND PUBLIC STAFF INVOLVEMENT IN PHASES 2 & 3**
11 **OF THE PROCESS**

12 **Q. SHOULD THE COMMISSION ESTABLISH A PROCESS IN THE**
13 **FINANCING ORDER TO BE ACTIVELY INVOLVED IN THE SECOND**
14 **AND THIRD PHASES OF THIS TYPE OF BOND TRANSACTION THAN**
15 **IT IS IN TRADITIONAL UTILITY DEBT OFFERINGS?**

16 A. Yes. For example, without Commission oversight – with the use of
17 Public Staff and its own independent experts and advisors reviewing these
18 contracts and negotiations – there would be no advocate for the ratepayers
19 in the process. There would be no one with a fiduciary duty to work in the
20 best interests of ratepayers, as more fully explained by Public Staff witness
21 Maher. Traditional utility debt has the shareholders at risk and is subject to
22 ongoing review. The Companies have a fiduciary duty to their shareholders

1 while they are concerned about overall customer rates. In this transaction,
2 the Commission issues an irrevocable financing order. Once the storm
3 recovery bonds are issued, the ratepayer bears all the costs directly, and
4 those costs are not subject to Commission review. It bears repeating -
5 every dollar in this transaction is a ratepayer dollar directly.

6 **Q. HAVE OTHER STATE COMMISSIONS ENSURED THAT THE**
7 **FINANCING COSTS ASSOCIATED WITH RATEPAYER-BACKED**
8 **BONDS, INCLUDING THE INTEREST RATES AND ALL OTHER**
9 **FINANCING COSTS, RESULTED IN THE LOWEST OVERALL COST TO**
10 **RATEPAYERS AS A CONDITION OF THE FINANCING ORDER?**

11 A. Yes, but not all. As described in greater detail below in this
12 testimony, some other state commissions have made the decision to remain
13 active in the Second and Third Phases of the process with a lowest cost
14 objective. They generally have used active independent financial advisors
15 and counsel. These commissions have instructed those financial advisors
16 as well as commission staff, along with representatives of the sponsoring
17 utility, to take part actively and in advance in all aspects of the structuring,
18 marketing, and pricing of Ratepayer-Backed Bonds.

1 **Q. HOW HAVE OTHER STATE COMMISSIONS ENSURED THAT**
2 **THE LOWEST COST TO THE RATEPAYERS HAS BEEN ACHIEVED?**

3 A. Other state commissions with active financial advisors have
4 instructed those financial advisors as well as commission staff to participate
5 actively and in advance in all aspects of the structuring, marketing and
6 pricing of Ratepayer-Backed Bonds. This has included reviewing the
7 earliest drafts of transactions documents and initial contacts with rating
8 agencies as well as investor presentations and the actual negotiations with
9 underwriters at the moment of pricing of the Ratepayer-Backed Bonds.
10 Fundamentally, the Companies' Joint Petition asks for approval of costs
11 based on estimates with no procedure for independent confirmation that the
12 most important costs, the interest costs, are in fact the lowest possible for
13 the benefit of ratepayers.

14 **Q. OTHER PUBLIC STAFF WITNESSES RECOMMEND THAT THE**
15 **FINANCING ORDER ESTABLISH A "BOND TEAM" THAT INCLUDES**
16 **THE COMMISSION, PUBLIC STAFF AND THE COMPANIES TO**
17 **PARTICIPATE IN THE STRUCTURING, MARKETING, AND PRICING OF**
18 **STORM RECOVERY BONDS. DO YOU AGREE?**

19 A. Yes, I agree. Public Staff witnesses attest to this point in their
20 testimonies, as shaped by their own extensive experience.

1 **THE FLORIDA PRECEDENT WITH DUKE ENERGY**
2 **Q. IN CONNECTION WITH THE ISSUANCE OF THE FIRST**
3 **SECURITIZED STORM RECOVERY BONDS FOR FLORIDA POWER**
4 **AND LIGHT IN 2007, DID THE FLORIDA PUBLIC SERVICE**
5 **COMMISSION (FPSC) FINANCING ORDER ESTABLISH A BOND TEAM**
6 **TO PARTICIPATE IN THE STRUCTURING, MARKETING AND PRICING**
7 **OF THOSE STORM RECOVERY BONDS?**

8 A. Yes. The commission established a post Financing Order / pre-bond
9 issuance review process that included a Bond Team.” The commission’s
10 financing order came after a fully contested case and consideration of a
11 detailed record discussing the core issues of concern about ratepayers and
12 the utility’s response.

13 **Q. WHEN DUKE ENERGY FLORIDA, LLC (DEF) APPLIED TO THE**
14 **FPSC FOR A FINANCING ORDER 10 YEARS LATER AUTHORIZING**
15 **THE ISSUANCE OF SECURITIZED RATEPAYER-BACKED BONDS, DID**
16 **DEF RECOMMEND THAT THE FPSC’S FINANCING ORDER**
17 **ESTABLISH A SIMILAR BOND TEAM TO PARTICIPATE IN THE**
18 **STRUCTURING, MARKETING AND PRICING OF THOSE RATEPAYER-**
19 **BACKED BONDS?**

20 A. No, they did not.

1 Q. AS THE FPSC'S FINANCIAL ADVISOR IN THAT 2015 DEF
2 PROCEEDING, DID SABER PARTNERS RECOMMEND THAT THE
3 FPSC'S FINANCING ORDER DIRECT THAT A BOND TEAM BE
4 FORMED TO PARTICIPATE IN THE STRUCTURING, MARKETING AND
5 PRICING OF THOSE STORM RECOVERY BONDS?

6 A. Yes.

7 Q. HOW DID THE FPSC RESOLVE THIS DIFFERENCE IN
8 RECOMMENDATIONS OF DEF AND THE FPSC'S FINANCIAL
9 ADVISOR CONCERNING FORMATION OF A BOND TEAM?

10 A. There was a joint stipulation of all parties. Prior to a potentially
11 contested public hearing, DEF entered into the Proposed Stipulations on
12 Financing Order Issues, dated October 13, 2015, including Issue 39:

13 "DEF's customers will be effectively
14 represented throughout the proposed
15 transaction. DEF, its structuring advisor,
16 and designated Commission staff and its
17 financial advisor will serve on the Bond
18 Team. One designated representative of
19 DEF and one designated representative of
20 the Commission shall be joint decision
21 makers for all matters concerning the
22 structuring, marketing, and pricing of the
23 bonds except for those recommendations
24 that in the sole view of DEF would expose
25 DEF or the SPE to securities law and other
26 potential liability (i.e., such as, but not
27 limited to, the making of any untrue
28 statement of a material fact or omission to
29 state a material fact required to be stated
30 therein or necessary in order to make the
31 statements made not misleading) or
32 contractual law liability (e.g., including but

1 not limited to terms and conditions of the
2 underwriter agreement(s)). The final
3 structure of the transaction, including
4 pricing, will be subject to review by the
5 Commission for the limited purpose of
6 ensuring that all requirements of law and
7 the Financing Order have been met.”
8

9 Fichera Exhibit 3 to this testimony is a copy of these “Proposed Stipulations
10 on Financing Order Issues.” These stipulations are reflected in the FPSC’s
11 Financing Order for the 2016 DEF securitized storm recovery bond
12 transaction.

13 **Q. FOR THE TRANSACTION PROPOSED BY THE JOINT PETITION,**
14 **WITNESSES KLEIN, SCHOENBLUM, SUTHERLAND, ABRAMSON,**
15 **AND MAHER RECOMMEND THAT THE COMMISSION’S FINANCING**
16 **ORDER ESTABLISH A BOND TEAM WHICH INCLUDES PUBLIC STAFF**
17 **BUT DOES NOT INCLUDE UNDERWRITERS. DO YOU AGREE?**

18 A. Yes, I agree. Underwriters are on the other side of the negotiating
19 table. They should not be part of internal discussions among the
20 Companies, the Public Staff and the Commission concerning how the Bond
21 Team will negotiate with the underwriters about interest costs.

1 **Q. THESE WITNESSES FURTHER RECOMMEND THAT THE BOND**
2 **TEAM BE A JOINT DECISION-MAKER WITH THE COMPANIES ON**
3 **MATTERS CONCERNING THE STRUCTURING, MARKETING AND**
4 **PRICING OF THE STORM RECOVERY BONDS. DO YOU AGREE?**

5 A. Yes, I agree. It is just common sense as well as a proven “best
6 practice.” The party that pays the bills and the party that must approve the
7 transactions should be part of the decision-making process.

8 **Q. WAS A DESIGNATED COMMISSIONER INVOLVED IN THE**
9 **FLORIDA BOND TEAM?**

10 A. Yes. Because there could be competing views in which a consensus
11 might not be reached (as in all committees), the DEF / FPSC Bond Team
12 provided for a designated Commissioner to be a member of the Bond Team,
13 with authority to cast the deciding vote if other members of the Bond Team
14 did not agree on any aspect of the structuring, marketing or pricing of the
15 Ratepayer-Backed Bonds. However, this aspect of the Florida Bond team
16 was never invoked because a consensus was reached on all aspects of the
17 structure, marketing and pricing of the bonds.

1 **Q. DO YOU RECOMMEND THAT THE FINANCING ORDER IN THIS**
2 **PROCEEDING INCLUDE A SIMILAR DECISION-MAKING PROCESS**
3 **WITHIN THE BOND TEAM?**

4 A. Yes. I recommend that the Commission's Financing Order in this
5 proceeding provide for a designated Commissioner to be a member of the
6 Bond Team, with authority to cast the deciding vote if other members of the
7 Bond Team do not agree on any aspect of the structuring, marketing or
8 pricing of the storm recovery bonds.

9 **THE COMPANIES BELIEVE THAT THE FLORIDA PRECEDENT**
10 **SHOULD NOT BE FOLLOWED**

11 **Q. IN HIS RESPONSE TO A PUBLIC STAFF DATA REQUEST, THE**
12 **COMPANIES' WITNESS ATKINS STATES: "PURSUANT TO**
13 **SECURITIES LAWS, DEP AND DEC WILL BE THE ISSUERS OF STORM**
14 **RECOVERY BONDS AND ANY SRB SECURITIES WITH LIABILITY**
15 **UNDER FEDERAL AND STATE SECURITIES LAWS. THEREFORE,**
16 **THERE IS NO 'SYMMETRY' AND IT IS NOT CORRECT TO COMPARE**
17 **THE ROLE OF DEP AND DEC AS PART OF ANY BOND TEAM, TO THE**
18 **EXTENT THERE IS A BOND TEAM, AND PUBLIC STAFF." DO YOU**
19 **AGREE?**

20 A. No. This is a distinction without a difference. As summarized above,
21 DEF made essentially this same argument to the Florida Commission in
22 connection with Ratepayer-Backed Bonds issued for DEF in 2016. But DEF

1 ultimately stipulated in that proceeding that other participants in the Bond
2 Team may be joint decision makers with DEF on all matters related to the
3 structuring, marketing and pricing of those Ratepayer-Backed Bonds. The
4 only exclusion was “except for those recommendations that in the sole view
5 of DEF would expose DEF or the SPE to securities law and other potential
6 liability (i.e., such as, but not limited to, the making of any untrue statement
7 of a material fact or omission to state a material fact required to be stated
8 therein or necessary in order to make the statements made not misleading)
9 or contractual law liability (e.g., including but not limited to terms and
10 conditions of the underwriter agreement(s)).” Saber Partners recommends
11 that similar provisions be included in the Commission’s financing order in
12 this proceeding assuming the Companies will be following the established
13 precedents from the DEF transaction.

14 **UNDERSTANDING UNDERWRITER INTERESTS IN THE**
15 **TRANSACTION**

16 **Q. IS THERE ANYTHING ABOUT THE STRUCTURE OF**
17 **INVESTMENT BANKING FIRMS THAT SERVE AS UNDERWRITERS**
18 **THAT THE COMMISSION SHOULD KNOW AND CONSIDER IN**
19 **EVALUATING THE JOINT PETITION?**

20 A. Yes. It is important to understand that underwriting firms are not
21 monoliths – single units all working together. They are organized into
22 different divisions, each managed and evaluated as a separate profit and
23 loss center. The compensation of investment bankers results from the

1 separate results of these different divisions. The divisions have different
2 customers. The banking division is distinct from the sales and trading
3 division. Within the sales and trading division, there is usually a distinction
4 between institutional and retail sales. Institutions are large money
5 managers.

6 Because income and profit come from transactions, there is tremendous
7 pressure to write “tickets,” to conduct transactions – and to do so quickly.
8 No bond sales and trading division that I know or have ever heard of is on
9 retainer, i.e., is paid a fee not associated with a transaction. Consequently,
10 the incentive is the more transactions a division completes, the quicker the
11 sales, the more income and profit there is to share among employees of
12 that division.

13 Divisions within an investment bank are further organized on the basis of
14 securities “products” they underwrite or trade. One of the biggest challenges
15 we have encountered with Ratepayer-Backed Bonds is getting the attention
16 and focus of the appropriate divisions across the banks to assist in
17 distributing the bonds at the lowest cost to ratepayers.

18 Public Staff witness Heller, who also worked in large underwriting firms
19 discusses this in more detail.

20 **Q. HOW IS THIS RELEVANT TO THE JOINT PETITION?**

21 A. The Joint Petition proposes a process that relies heavily on the
22 “professional judgement” of underwriters to achieve the lowest storm
23 recovery charges to ratepayers. It is very light on discussion of how to gain

1 the greatest value from the Financing Order from investors. However, the
2 salespeople and the traders who buy the bonds from the issuer to re-sell
3 the storm recovery bonds to their investor clients do not have a duty to act
4 in the best interests of the ratepayer. That's not their job despite the
5 Companies assertion. Their job is described in their underwriting
6 agreement as witness Maher discusses in more detail and explains what
7 that means for ratepayers in this transaction.

8 It has been my experience both as an employee of major investment banks
9 for 17 years as well as in conversations, discussions with individuals
10 currently employed at major investment banks, that they are compensated
11 by re-selling securities and re-selling them quickly. Their primary clients are
12 investors who are in the market frequently buying and selling securities.
13 This "flow" of transactions is critical to the financial interests of the firm and
14 the individuals. Underwriters depend on these investors on a daily basis
15 versus the infrequent issuer of Ratepayer-Backed Bonds. Remember, in
16 the past 5 years only 3 of these transactions came to market. It just does
17 not get the focus of the firm in a way that benefits ratepayers when a new
18 transaction comes to market.

19 The Companies conceded in a response to a Public Staff data request that
20 underwriters, as do all participants in financing transactions, work in their
21 own best interests consistent with the contractual and legal obligations
22 under which they operate. As Public Staff witness Maher points out, their

1 contractual and legal obligations are clearly explained and do not include
2 the best interests of the ratepayers.

3 **Q. WHAT IS THE DIFFERENCE BETWEEN SALESPEOPLE AND**
4 **TRADERS?**

5 A. Salespeople interact with investors directly, like an individual's
6 personal broker. Traders decide how to use the investment bank's capital
7 to buy and sell securities for the investment bank's own account. Traders
8 decide on the actual prices and yields at which they are willing to purchase
9 or sell fixed-income debt securities.

10 There is a plethora of products, and both traders and investors have limited
11 time. The compensation system for both salespeople and traders
12 encourages efficiency – make the maximum amount of profit for the division
13 of the investment bank in the year and be paid “on performance.”
14 Performance (profit) is the bottom-line.

15 **Q. WHAT IS THE BIGGEST CHALLENGE IN DEALING WITH**
16 **UNDERWRITERS?**

17 A. The biggest challenge is getting underwriters to spend the time and
18 energy to create maximum value for the ratepayer. I know it can be done
19 because I have seen it from both sides - both as an underwriter and as
20 financial advisor to issuers and to regulators. It just is not easy. The

- 1 pressure is to do the deal, to take the offer that is already on the table.
2 Volume and spread are the key drivers.

3 **BEST PRACTICES: RECOMMENDED PROCEDURES**

4 **Q. WHAT ARE THE MOST IMPORTANT BEST PRACTICES FOR**
5 **NORTH CAROLINA'S FIRST RATEPAYER-BACKED BOND**
6 **TRANSACTION AND IN ESTABLISHING A PROGRAM?**

7 A. Following proven best practices would benefit North Carolina
8 ratepayers in establishing the proposed storm recovery bond program and
9 in the initial public offering of Ratepayer-Backed bonds as witnesses
10 Abramson, Klein, Schoenblum, Maher and Sutherland have explained. The
11 ones I would highlight are:

- 12 1. The Commission should use its authority to include terms and conditions
13 in the Financing Order to protect the ratepayer in structuring, marketing
14 and pricing the storm recovery bonds.
- 15 2. The Commission and ratepayer advocates need to collaborate with the
16 Companies and additional members of a Bond Team to ensure they
17 achieve a "lowest storm recovery charge" standard, relying on the
18 expertise of independent financial advisors like Saber Partners to
19 discern just how that can be achieved. Independent means no financial
20 interest in the bond proceeds or the bonds themselves and with a duty
21 to loyalty– a fiduciary responsibility to the ratepayer – the Commission
22 and the Public Staff.

1 3. After pricing but before closing, the Companies, the Underwriters and
2 the Public Staff's financial advisor each should certify that the lowest
3 storm recovery charge standard has been achieved, so the Commission
4 has time to stop the transaction if it determines that standard is not
5 achieved.

6 **COMMENT ON THE COMPANIES' RESPONSES TO CERTAIN DATA**
7 **REQUESTS**

8 **Q. IN THE JOINT PETITION AND IN RESPONSES TO PUBLIC**
9 **STAFF'S DATA REQUESTS, DID ANYTHING SURPRISE YOU?**

10 A. Yes. The Companies failed to recommend that the Commission
11 follow many of the best practices that DEF agreed to be included in the 2015
12 securitization Financing Order issued by the FPSC.
13 For example, that 2015 FPSC Financing Order required that the "marketing"
14 (as well as the "structuring" and "pricing") of the Ratepayer-Banked Bonds
15 result in the lowest securitization charge consistent with market conditions
16 at the time of pricing. Here, the Companies propose that the "lowest storm
17 recovery charge" standard be based only on "structuring and pricing"
18 without regard to "marketing" efforts in connection with the proposed storm
19 recovery bonds. This does not make sense. Consider the analogy of a
20 family selling its home. Does the family list with only one broker or many?
21 How are potential buyers should be contacted? How does the family
22 present the home? The best price the family will get will be determined by
23 how well the house is marketed. If the family just wants to sell quickly and

1 does not care about getting the best price, then the family will likely sell the
2 home quickly. Here, we have a duty to get the ratepayer the lowest cost on
3 a bond structure that has been infrequently sold and is not well understood,
4 so marketing will be essential. For the Companies to leave “marketing” out
5 of their proposal – even though it was included in the successful FPSC
6 Financing Order issued to DEF – is a major deficiency and should be
7 corrected.

8 As a second example, as financial advisor to the FPSC and to other
9 regulators in connection with other prior Ratepayer-Backed Bond
10 transactions, Saber Partners pioneered the practice of requiring
11 certifications or opinions in writing, without material qualifications,² from
12 underwriters. These written certifications say the structuring, marketing and
13 pricing of Ratepayer-Backed Bonds in fact resulted in the lowest
14 securitization charges consistent with market conditions at the time of
15 pricing and the terms of the Financing Order. The Companies do not
16 propose that underwriters be required to deliver such certifications or
17 opinions. For additional information about these compliance certifications,
18 see the testimony of Public Staff witnesses Schoenblum and Moore.

² Despite an explicit lowest cost standard in the New Jersey statute, from 2001 - 2004, the utilities, Underwriters, and the New Jersey Commission's financial advisors were allowed to place significant qualifications in their “lowest cost” certifications. In contrast, for the 2005 transaction for the benefit of Public Service Electric & Gas (PSE&G), the New Jersey Commission and its financial advisor eliminated these significant qualifications by adopting the Texas Commission financing order certification model. As shown on Sutherland Exhibit 4, the Spread for the 2005 PSE&G transaction was considerably tighter (i.e., less expensive to ratepayers) than any previous Ratepayer-Backed Bond transaction completed in New Jersey. See Staff Issues Decision Memoranda Document # 04068 May 9, 2006 in Docket No. 060038-EI- Petition for issuance of a storm recovery financing order by Florida Power & Light Company.

1 One key aspect of a written certification is not to have any “material
2 qualifications.” This means statements, conditions or assumptions that
3 dilute the meaning and intent of the certification or opinion. In its 2006 FP&L
4 storm securitization Financing Order, the FPSC examined certifications that
5 New Jersey Board of Public Utilities required of its financial advisor on
6 Ratepayer-Backed Bond offerings versus certifications the PUCT required
7 of its financial advisor. It found that the New Jersey form of certification was
8 weakened by the qualifications the advisor put in the certification. When
9 the Ratepayer-Backed Bond pricings of New Jersey and Texas were
10 compared – though each had certification letters – the Texas transactions
11 got consistently lower credit spreads to benchmark issues. This meant
12 Texas ratepayers paid less and indeed got the lowest costs and lowest
13 securitization charge at the time of pricing. A study of Texas versus New
14 Jersey Ratepayer-Backed Bond pricings by Barclays Bank in 2005
15 confirmed this outcome. A copy of that study was provided to Saber
16 Partners.

1 Q. WAS IT EASY TO PERSUADE UNDERWRITERS TO DELIVER
2 THOSE CERTIFICATIONS FOR THE 2016 DEF TRANSACTION OR
3 OTHER PRIOR RATEPAYER-BACKED BOND TRANSACTIONS
4 WHERE SABER SERVED AS FINANCIAL ADVISOR TO THE
5 REGULATOR?

6 A. No. Underwriters were concerned about their liability from making
7 the certification.

8 Q. WAS THAT A VALID CONCERN?

9 A. Yes, in part. It was the driving motivation for Saber Partners to seek
10 the confirming certification or opinion. It is relatively easy for bond issuers
11 to get underwriters to say something orally about market conditions and the
12 results of the underwriters' efforts in structuring, marketing and pricing
13 publicly-offered securities. It is another thing to get the underwriters to "put
14 that that in writing."

1 Q. AFTER THE PRICING OF THE STORM RECOVERY BONDS, THE
2 COMPANIES ARE CALLED UPON TO CERTIFY THAT THE
3 STRUCTURING AND PRICING OF THE BONDS RESULTED IN THE
4 LOWEST STORM RECOVERY CHARGES CONSISTENT WITH
5 MARKET CONDITIONS AT THE TIME (SEE PROPOSED FINANCING
6 ORDER, APPENDIX C). WHY IS IT IMPORTANT THAT THE
7 COMPANIES DELIVER THESE CONFIRMING CERTIFICATIONS?

8 A. Representatives of the Companies will be involved in the decisions
9 related to the structuring, marketing and pricing of storm recovery bonds. It
10 is only prudent to expect that the Companies, as Joint Petitioners, will also
11 deliver certificates confirming that the “lowest storm recovery charge”
12 requirement set forth in the Financing Order has, in fact, been met.

13 Q. IS THE FINANCING ORDER PROPOSED BY THE JOINT
14 PETITION AMBIGUOUS CONCERNING WHETHER THE COMPANIES
15 WILL BE REQUIRED TO DELIVER THESE CONFIRMING
16 CERTIFICATIONS?

17 A. Yes. Public Staff witness Schoenblum’s testimony reinforces this.

1 Q. DO YOU ALSO AGREE THAT THAT IT IS APPROPRIATE FOR
 2 THESE CERTIFICATIONS TO CONFIRM THAT “MARKETING” OF THE
 3 STORM RECOVERY BONDS RESULTED IN THE “LOWEST STORM
 4 RECOVERY CHARGE”?

5 A. Yes. Public Staff witnesses Schoenblum and Klein concur.

6 Q. IN RESPONDING TO A PUBLIC STAFF DATA REQUEST,
 7 COMPANIES WITNESS ATKINS STATED THAT THE DRAFT
 8 FINANCING ORDER FOR THE PROPOSED DEC AND DEP
 9 TRANSACTION WERE DESIGNED TO COMPLY WITH THE NORTH
 10 CAROLINA STATUTORY REQUIREMENTS, WHICH DID NOT INCLUDE
 11 A ROLE FOR A DESIGNATED REPRESENTATIVE IN THE POST-
 12 FINANCING ORDER DECISIONS CONCERNING THE ‘MARKETING’ OF
 13 THE SECURITIES BEING OFFERED IN THE TRANSACTION. HE WENT
 14 ON FURTHER TO STATE THAT COMPARISONS TO THE 2016 DEF
 15 TRANSACTION ARE NOT APPROPRIATE AS THAT TRANSACTION
 16 CONCERNED A DIFFERENT UTILITY REGULATED BY A DIFFERENT
 17 COMMISSION UNDER A DIFFERENT STATUTE. DO YOU AGREE WITH
 18 WITNESS ATKINS?

19 A. No. Relevant provisions of the Florida statute and the North Carolina
 20 statute are essentially the same.

21 F.S. § 366.95(2)(c)2. states:

22 **In a financing order issued to an electric**
 23 **utility, the commission shall:**

24 * * *

1 b. Determine if the proposed structuring,
 2 expected pricing, and financing costs of the
 3 nuclear asset-recovery bonds have a
 4 significant likelihood of resulting in lower
 5 overall costs or would avoid or significantly
 6 mitigate rate impacts to customers as
 7 compared with the traditional method of
 8 financing and recovering nuclear asset-
 9 recovery costs. . . .;

* * *

10
 11 **i. Include any other conditions that the**
 12 **commission considers appropriate and**
 13 **that are authorized by this section.”**

14
 15 N.C.G.S. § 62-172(b)(3)b. states:

16 **“A financing order issued by the**
 17 **Commission to a public utility shall**
 18 **include all of the following elements:**

* * *

19
 20 3. A finding that the structuring and pricing
 21 of the storm recovery bonds are reasonably
 22 expected to result in the lowest storm
 23 recovery charges consistent with market
 24 conditions at the time the storm recovery
 25 bonds are priced and the terms set forth in
 26 such financing order.

* * *

27
 28 **12. Any other conditions not otherwise**
 29 **inconsistent with this section that the**
 30 **Commission determines are**
 31 **appropriate.”**

32

1 Q. PUBLIC STAFF WITNESSES SCHOENBLUM AND KLEIN
2 TESTIFY THAT, IN THEIR VIEW, THE COMMISSION SHOULD REQUIRE
3 THESE CONFIRMING “LOWEST STORM RECOVERY CHARGE”
4 CERTIFICATIONS NOT ONLY FROM THE COMPANIES, BUT ALSO
5 FROM THE BOOKRUNNING UNDERWRITER(S) AND FROM THE
6 COMMISSION’S OR PUBLIC STAFF’S INDEPENDENT FINANCIAL
7 ADVISOR. IF THE COMPANIES DELIVER THESE CERTIFICATIONS,
8 WHY ARE “LOWEST STORM RECOVERY CHARGE” CERTIFICATIONS
9 ALSO NEEDED FROM THE BOOKRUNNING UNDERWRITER(S) AND
10 AN INDEPENDENT FINANCIAL ADVISOR?

11 A. An independent certification from someone with a duty to the
12 ratepayers – the party that is paying the costs - is prudent and consistent
13 with how many other financial transactions are done. By law, after the
14 storm recovery bonds are issued and the Companies receive the net
15 proceeds, there is no further review of the transaction possible by the
16 Commission. The Companies have a financial incentive to receive the
17 proceeds as quickly and effortlessly as possible, with no liability for the
18 resulting storm recovery charges and arguably no liability in giving these
19 certifications. And the Companies might truly believe they got the best deal.
20 However, despite their best efforts, the Companies might not have access
21 to all information that is material to determining whether the “lowest storm
22 recovery charges” in fact were achieved. This is particularly true of
23 information about communications between the underwriters’ salespersons

1 and potential investors, both on the day of pricing and also during the weeks
2 leading up to pricing. For that reason, in my view, it also is important that
3 the bookrunning underwriter(s) also deliver a “lowest storm recovery
4 charge” certification after the storm recovery bonds are priced and before
5 they are issued.

6 **Q. IN RESPONSE TO A PUBLIC STAFF DATA REQUEST, WITNESS**
7 **HEATH STATED THAT THE SRB SECURITIES WILL NOT BE ISSUED**
8 **BY CUSTOMERS, SO IT IS INAPPROPRIATE TO SUGGEST THAT**
9 **CUSTOMERS WOULD NEGOTIATE WITH UNDERWRITERS. HE WENT**
10 **ON TO STATE THAT THE COMPANIES ARE NOT AWARE OF ANY**
11 **SECURITIES OFFERINGS WHERE RATEPAYERS NEGOTIATED**
12 **DIRECTLY WITH UNDERWRITERS. DO YOU AGREE?**

13 A. No. That is a distinction that is without a difference. Newly-formed
14 limited purpose subsidiaries will be the issuers of storm recovery bonds,
15 and a grantor trust wholly-owned by Duke Energy Corporation would be the
16 issuer of any SRB Securities. The issuers will be responsible to pay all debt
17 service and other financing costs with respect to the storm recovery bonds
18 – but only from specifically identified resources that will consist principally
19 of storm recovery charge collections from customers. The transaction will
20 be set up so that debt service and other financing costs will be a complete
21 passthrough to the ratepayer. Investors cannot look to DEC, DEP or Duke
22 Energy Corporation to get a penny. Investors may look only to the issuers,

1 and the issuers will be obligated to make payments only to the extent of
2 amounts held by a bond trustee in a "Collection Account" which will consist
3 principally of collections of storm recovery charge revenues from
4 customers. In addition, the issuers will own storm recovery property, which
5 includes the right to bill, charge and collect storm recovery charges and to
6 require the Commission to adjust the storm recovery charge to whatever
7 level is necessary to repay the investors on time.

8 This is fundamentally different from when the Companies themselves issue
9 debt securities. There the bondholders can go after the assets of the entire
10 operating utility company if it's a first mortgage bond. Unsecured creditors
11 might have to wait in line, but they can sue the operating utility for payment.
12 Bankruptcy is a real risk for operating utilities. Neither DEC nor DEP can
13 force the Commission to raise customer rates immediately and to whatever
14 level might be necessary to pay their creditors. It is just not the same.

15 **Q. DO YOU HAVE ANY CONCERNS WITH THE PROPOSED**
16 **GRANTOR TRUST STRUCTURE THAT COMPANIES WITNESS**
17 **ATKINS PROPOSES TO BE USED THAT COMBINES THE STORM**
18 **RECOVERY BOND ISSUANCES OF BOTH DUKE ENERGY**
19 **CAROLINAS AND DUKE ENERGY PROGRESS INTO A SINGLE**
20 **SECURITY?**

21 A. I believe all options should be explored that may produce the lowest
22 cost to the ratepayer. However, the structure has only been used once in

1 the last 15 years, and that was for FirstEnergy of Ohio. Other utilities in
2 Louisiana and West Virginia that have two affiliated companies with the
3 option of using that structure did not choose it. I believe it adds a layer of
4 complexity to the sale of the Ratepayer-Backed Bonds that may cost
5 ratepayers more. While the Companies believe that it is not complex, the
6 lead bookrunning manager and structuring advisor of the FirstEnergy of
7 Ohio transaction (Goldman Sachs) informed the Companies (in their
8 response to the Companies request for proposals for a structuring advisor)
9 that they did not recommend the structure for the Companies and called the
10 grantor trust bond structure “complex.”

11 Moreover, according to a report by FirstSouthwest (attached to this
12 testimony as Fichera Exhibit 4), the independent financial advisor to the
13 Public Utility Commission of Ohio on the transaction at the time, there were
14 only eight investors in each of the tranches of the \$444 million Ratepayer-
15 Backed Bond issuance. Notably, that transaction did not have a lowest cost
16 to the ratepayer standard in the authorizing legislation nor the Financing
17 Order authorizing the Ratepayer-Backed Bond sale. These facts raise
18 serious questions as to whether this structure would be in the best interest
19 of the Companies’ ratepayers.

20 Finally, the main reason cited by witness Atkins for using the combined
21 grantor trust structure – to make the bonds eligible in size for inclusion in
22 the Bloomberg Barclays Aggregate Bond Index” - is dubious at best. There
23 is no supporting evidence that this index, as opposed to other indices

1 followed by utility and corporate bond investors, would have any effect on
2 lowering the interest rate on the bonds. A review of witness Atkins' previous
3 testimony on behalf of other utilities in Ratepayer-Backed Bond transactions
4 found no mention of the "Aggregate Bond Index" as a material factor in
5 structuring, marketing or pricing the bonds. The Companies did admit that
6 the Corporate Utilities Bond Index was an important factor that could lower
7 ratepayer costs. However, to be eligible for the Aggregate Bond Index the
8 Companies would have to promote the storm recovery bonds as "asset
9 backed securities" even though the Companies say the storm recovery
10 bonds would be structured like the DEF bonds as "not asset-backed
11 securities as defined by SEC Regulation AB." So, besides complexity, the
12 approach seems to add confusion. Neither of these will likely lower
13 ratepayer costs in negotiations with investors.

14 If the Commission's Financing Order allows the possibility for using a
15 grantor trust structure, however, this structure should be studied by the
16 proposed Bond Team with further analysis by Public Staff and its
17 independent advisor, given the lack of any evidence supporting the value of
18 such an option.

1 **Q. WHY IS MARKETING SO IMPORTANT? DO NOT MOST MAJOR**
2 **UNDERWRITERS AND INVESTORS UNDERSTAND WHAT**
3 **RATEPAYER-BACKED BONDS ARE SO THAT VERY LITTLE TIME**
4 **NEEDS TO BE SPENT ON INVESTOR EDUCATION?**

5 A. Because Ratepayer-Backed Bond issuances have been infrequent
6 and often mischaracterized by Underwriters and others, I do not believe
7 there is a thorough understanding of the nature of the credit so that they are
8 properly valued. The best example of the confusion associated with
9 Ratepayer-Backed Bonds is a research report that was done by Wells Fargo
10 in 2013 (attached as Fichera Exhibit 5). Wells Fargo was a co-managing
11 Underwriter on an Ohio Power Ratepayer-Backed Bond offering and was
12 the sole Underwriter of the Florida Power & Light storm securitization bonds
13 in 2007. However, the research report described the transaction as a “utility
14 receivables” transaction. Receivables are a core part of the “asset-backed
15 securities” market and involve many complexities and risks. However,
16 receivables are not part of any Ratepayer-Backed Bond structure. There
17 are no receivables pledged to the bondholders or part of the collateral for
18 the bonds.

19 Directly on point, for example, the prospectus for the Florida Power & Light
20 storm recovery bond transaction stated that “[s]torm-recovery property is
21 not a receivable, and the principal credit supporting the related series of

1 bonds is not a pool of receivables.”³ The same will be true with North
2 Carolina storm recovery property. Witness Heller discusses this investor
3 and underwriter confusion in his testimony. This is one of the reasons he
4 says they should not be treated as “asset-backed securities.”
5 But, the fact that a major investment banking firm in a 10-page report
6 described it as a “utility receivables” transaction is a concern and a
7 challenge. While the report got many things right, it got this core issue
8 wrong. This is symptomatic of a larger marketing problem that we have
9 confronted over and over again in the 20 years that Saber Partners has
10 been involved in the Ratepayer-Backed Bond market. Underwriters are not
11 familiar with the structure and attempt to use shorthand or comparisons to
12 things they are familiar with but are not part of the unique and extraordinary
13 security that a Ratepayer-Backed Bond has. While the rating agencies dryly
14 describe accurately the structure and credit, salespeople often get it wrong.
15 That is another reason why a representative of the ratepayer needs to be
16 at the negotiating table and why the Bond Team proposal is a best practice.

17 **COMPARISON TO OTHER SECURITIES RELEVANT TO**
18 **CONSIDERING THE JOINT PETITION**

19 **Q. IS A COMPARISON TO OTHER SECURITIES IMPORTANT TO**
20 **RATEPAYERS?**

21 A. Yes. As discussed in greater detail by Public Staff witnesses
22 Schoenblum, Sutherland, Heller, Abramson and Maher, it is important to

³ https://www.sec.gov/Archives/edgar/data/37634/000090514807003876/efc7-1376_424b5.txt at page 6.

1 compare storm-recovery bonds to other comparable securities in the market
2 to determine whether ratepayers have received all the benefits from
3 securitized storm recovery bonds, the legislation and the Financing Order,
4 and to have a benchmark for success. All securities price in relation to other
5 securities. Only by knowing and examining these and other factors can one
6 determine whether a Ratepayer-Backed Bond transaction has been
7 successful or not.

8 **Q. PUBLIC STAFF WITNESSES HELLER AND SUTHERLAND**
9 **RECOMMEND THAT THE STORM RECOVERY BONDS BE**
10 **STRUCTURED AND MARKETED AS “CORPORATE DEBT**
11 **SECURITIES” AND NOT AS “ASSET-BACKED SECURITIES.” DO YOU**
12 **AGREE?**

13 A. Yes, I agree.

14 **Q. HOW WILL MARKETING AND INVESTOR EDUCATION AFFECT**
15 **THE COST OF STORM-RECOVERY BONDS?**

16 A. As discussed in the testimony of Public Staff witness Schoenblum,
17 in issuing bonds, there are specific rules and regulations to follow,
18 disclosure and marketing documents to be filed with regulators, and the
19 bonds will compete with multiple alternative investment opportunities. But
20 investors' fundamental valuation comes from an understanding of the credit,
21 its liquidity, “relative value” and the functioning of the capital markets.

1 Accurate market education does not happen by itself. It usually occurs only
2 if undertaken and pursued vigorously by those who have a stake in the
3 outcome. For example, the Companies, as well as almost all other
4 corporations, spend a great deal of shareholder resources in promoting and
5 educating the market for their stock and their debt securities. The
6 management invests this time and energy because it believes that from true
7 market education and a better understanding of its company, the valuation
8 of the company's stock and debt securities will increase for the benefit of
9 shareholders. The management also targets efforts at lenders to lower the
10 company's borrowing costs because it expects to need debt capital on an
11 ongoing basis.

12 With storm-recovery bonds, because the Companies are not responsible for
13 any costs of borrowing, as it otherwise would be in a traditional debt offering,
14 the Companies have no immediate stake in the outcome other than to
15 receive the cash and improve their balance sheets as quickly as possible.
16 Moreover, the transaction is likely viewed from the Companies' perspective
17 as a one-time offering, or, at the very least, an infrequent offering, so their
18 need to make a concerted effort to educate the market regarding the
19 benefits of storm-recovery bonds is diminished.

20 While well intentioned, the Companies' management also is distracted by
21 independent concerns stemming from the fact that its current debt is a direct
22 burden on revenues that are available to its shareholders, and storm-
23 recovery bonds are not. Therefore, there is little incentive for the

1 Companies to invest time and effort in educating the market, expanding the
2 market, or creating as broad a competition as possible for this or other
3 storm-recovery bond issuances.

4 As the beneficiary of the storm-recovery bond issue, the Companies can
5 and should work collaboratively with the Commission, Public Staff and
6 advisors to achieve a successful lowest storm recovery charge and lowest
7 cost financing. The Bond Team process, with the Commission having
8 access to independent advisors with a duty of loyalty and care to the
9 ratepayer (in this case provided by Public Staff) , can and should take a co-
10 leadership role with the Companies in marketing and in investor education
11 efforts. A joint and collaborative effort can best serve the interests of
12 ratepayers while fully addressing the financing needs of the utility.

13 **IMPORTANCE OF PHASES 2 &3 STRUCTURING, MARKETING AND**
14 **PRICING**

15 **Q. HAVE COMMISSIONS IN OTHER STATES BEEN ACTIVELY**
16 **INVOLVED IN THE STRUCTURING, MARKETING, AND PRICING OF**
17 **THESE TRANSACTIONS AFTER THE ISSUANCE OF THE FINANCING**
18 **ORDERS?**

19 A. Yes. Commissions in Texas, Florida, West Virginia, New Jersey, and
20 California and Louisiana have been actively involved in the structuring,
21 marketing and pricing of Ratepayer-Backed Bonds. Significantly, the
22 California Public Utilities Commission, which was one of the first states to
23 sponsor Ratepayer-Backed Bonds, initially did not participate actively after

1 issuing its Financing Orders in 1997 and 1998. However, when a second
2 round of Ratepayer-Backed Bonds was authorized in 2004, the California
3 Commission created an active role for a Commission financing team to
4 approve post-Financing Order matters. They confirmed this role again in
5 November 2020 in a Financing Order for Southern California Edison
6 Company,⁴ the California Commission's first Financing Order in 16 years.
7 The PUCT has had the most active post-Financing Order participation.
8 Two transactions illustrate the results that can be achieved by an active and
9 involved commission in the structuring, marketing and pricing of Ratepayer-
10 Backed Bonds. In September 2005, Public Service Electric and Gas
11 Company of New Jersey sponsored the issuance of \$102 million of
12 Ratepayer-Backed Bonds. Saber served as financial advisor to the New
13 Jersey Commission, and Credit Suisse (CS) was the lead underwriter.
14 Normally a transaction of this size might have been difficult to sell because
15 of its small size relative to other competing investments.
16 However, according to a report written by CS to the New Jersey
17 Commission,

18 “The extensive marketing of these bonds
19 conducted by CS, Barclays and M.R. Beal,
20 with active participation by Saber, led to the
21 unprecedented (low) pricing spreads,
22 despite the disadvantage of relatively small
23 tranche sizes.”
24

⁴ See *California Current* CPUC Judge Adds Ratepayer Protections to \$337M SCE Bond
<http://cacurrent.com/subscriber/archives/41788>.

1 In December 2005, CenterPoint Energy of Texas initially offered \$1.2 billion
2 of Ratepayer-Backed Bonds to the market. Saber was the financial advisor
3 with joint decision-making responsibility with the issuer. The PUCT acted
4 by and through the financial advisor. CS was one of the bookrunning
5 underwriters. In this case, the large size of the transaction, coupled with
6 the timing of the issuance at the end of the year (which traditionally is not a
7 good time to sell securities) posed special challenges. Nevertheless, the
8 Ratepayer-Backed Bonds received worldwide investor demand at record-
9 low credit spreads. The transaction was increased to \$1.85 billion with over
10 one-third of the bonds being sold to foreign investors for the first time ever.
11 This transaction was also notable because of the large amount of bonds
12 sold with very long maturities which are the type of bonds most costly to
13 ratepayers. Yet, the credit spread levels achieved by the PUCT for
14 ratepayers through these Texas Ratepayer-Backed Bonds on the longest
15 maturities were significantly below all other previously offered Ratepayer-
16 Backed Bonds in any state.

17 **Q. IN TEXAS, DID SABER PARTNERS SERVE AS FINANCIAL**
18 **ADVISOR TO THE PUCT IN CONNECTION WITH \$1,739,700,000**
19 **PRINCIPAL AMOUNT OF RATEPAYER-BACKED BONDS ISSUED IN**
20 **2006 FOR AEP TEXAS CENTRAL COMPANY?**

21 A. Yes. That issuance of Ratepayer-Backed Bonds consisted of five
22 separate sequential-pay tranches. Each tranche was separately priced.

1 Attached as Fichera Exhibit 2 is a copy of page 49 of the "Pricing Book" for
2 that Ratepayer-Backed Bond transaction. This Pricing Book is dated
3 October 4, 2006, and was prepared by CS, the bookrunning underwriter, as
4 a report to the sponsoring utility and to the PUCT about the success in
5 pricing each of the five tranches.

6 **Q. WHEN THESE RATEPAYER-BACKED BONDS WERE PRICED,**
7 **AND THE UNDERWRITERS ENTERED INTO AN UNDERWRITING**
8 **AGREEMENT COMMITTING TO PURCHASE ALL \$1,739,700,000**
9 **PRINCIPAL AMOUNT OF RATEPAYER-BACKED BONDS, DID THE**
10 **UNDERWRITERS HAVE ORDERS FROM INVESTORS FOR ALL THESE**
11 **BONDS?**

12 A. No. At final pricing, page 49 of the "Pricing Book" Saber Partners
13 requested that the underwriters prepare to memorialize the transaction
14 process, reports that the underwriters had orders for more than 100% of
15 tranches 1, 2, 3 and 5, but for only 96% of tranche 4. Tranche 4 had a
16 weighted average life of 10.0 years and a principal amount of \$437,000,000.

1 Q. IF THE UNDERWRITERS WERE NOT ABLE TO FIND
2 INVESTORS BETWEEN PRICING AND THE OCTOBER 11, 2006
3 CLOSING DATE, WHO WOULD BE OBLIGATED TO PURCHASE THE
4 \$17,480,000 OF BONDS THAT HAD NOT BEEN PRE-SOLD TO
5 INVESTORS?

6 A. The underwriters would be required to use their own capital to
7 purchase this \$17,480,000 of bonds at the initial public offering price (less
8 the agreed upon underwriter's discount set forth in the Underwriting
9 Agreement).

10 Q. DID THE TEXAS SECURITIZATION STATUTE RESEMBLE N.C.
11 G.S. § 62-172 IN REQUIRING THAT THOSE RATEPAYER-BACKED
12 BONDS BE PRICED SO AS TO PRODUCE THE LOWEST
13 SECURITIZATION CHARGES CONSISTENT WITH MARKET
14 CONDITIONS AT THE TIME OF PRICING?

15 A. Yes. Section 39.301 of the Texas Public Utility Regulatory Act
16 states: "The commission shall ensure that the structuring and pricing of the
17 transition bonds result in the lowest transition bond charges consistent with
18 market conditions and the terms of the Financing Order."

1 Q. DID OUTSIDE LEGAL COUNSEL TO AEP TEXAS CENTRAL
2 DELIVER ITS OPINION THAT THOSE RATEPAYER-BACKED BONDS
3 WERE VALIDLY ISSUED?

4 A. Yes. A copy of that legal opinion delivered by Sidley Austin LLP was
5 filed with the SEC and can be found at
6 [https://www.sec.gov/Archives/edgar/data/18734/000119312506185414/de](https://www.sec.gov/Archives/edgar/data/18734/000119312506185414/dex51.htm)
7 [x51.htm](https://www.sec.gov/Archives/edgar/data/18734/000119312506185414/dex51.htm).

8 Q. IN RESPONDING TO A PUBLIC STAFF DATA REQUEST,
9 COMPANIES WITNESS ATKINS STATED THAT A MARKET-CLEARING
10 PRICING WOULD RESULT IN INTEREST RATES FOR THE SRB
11 SECURITIES THAT ARE CONSISTENT WITH MARKET CONDITIONS
12 AT THE TIME OF PRICING. HE WENT ON TO STATE THAT INTEREST
13 RATES THAT ARE SUBSIDIZED BY PRIVATE COMPANIES, WHETHER
14 UNDERWRITER FIRMS OR THE COMPANIES, THROUGH THE
15 PURCHASE OR RETENTION OF UNSOLD UTILITY SECURITIZATION
16 BONDS, ARE NOT CONSISTENT WITH MARKET CONDITIONS AT THE
17 TIME OF PRICING, AND THEREFORE INCONSISTENT WITH N.C. GEN.
18 STAT. § 62-172. DO YOU AGREE WITH WITNESS ATKINS?

19 A. No. I believe the Pricing Book for the 2006 AEP Texas Central
20 Ratepayer-Backed Bond transaction, together with the approving legal
21 opinion delivered by Sidley Austin LLP, illustrates that an underwriter's
22 purchase or retention of any unsold storm recovery bonds would be

1 consistent with market conditions at the time of pricing, and therefore
2 consistent with N.C.G.S. § 62-172.

3 **Q. DOES A “LOWEST COST” AND “LOWEST SECURITIZATION**
4 **CHARGE” STANDARD CREATE MORE COSTS FOR RATEPAYERS**
5 **THAN A LESSER STANDARD?**

6 A. No. As explained in the testimony of Public Staff witness
7 Schoenblum, pursuing a lowest cost and lowest securitization charge
8 standard might require transaction participants to work harder, but not at a
9 higher net economic cost. Hard work is an investment that always pays off.
10 Consider that the Companies propose almost \$12 million in issuance
11 expenses. It is appropriate to expect the best possible outcome for such
12 costs, especially from the underwriters. Otherwise, waste and inefficiency
13 might arise from the process. Indeed, not pursuing the lowest cost almost
14 guarantees higher costs to the ratepayer because there is no incentive or
15 accountability to get anything better.

16 Among the transaction costs, the greatest economic cost to ratepayers is
17 the interest rate on the bonds which ratepayers will be paying for the entire
18 term to maturity. This dwarfs any single up-front transaction cost. One
19 eighth of one per cent of \$1 billion outstanding for about 7.5 years will cost
20 ratepayers \$9.4 million in nominal dollars. For a longer maturities such as
21 up to 20 years, this amount would be even more. For the reasons outlined
22 in the testimony of Public Staff witness Schoenblum, “reasonable” is not an

1 appropriate standard to apply, especially when the potential cost is so
2 substantial. Moreover, without meaningful involvement in real time, there
3 will be no way for the Commission to know that the transaction was priced
4 at the lowest interest rate possible.

5 This is one reason why care needs to be taken, in cooperation with the
6 Companies, in selecting experienced transaction participants and others. It
7 is essential to put together a team which shares a similar objective and
8 commitment to excellence, which can provide economies of scale and
9 which is responsive to competitive pressures and economic incentives. If
10 the economic incentives are properly aligned with proper oversight, then
11 underwriters, counsel, advisors and others will work in the most cost-
12 effective, collaborative manner with the Commission and the Companies to
13 achieve the lowest storm recovery charge and lowest cost objective. If there
14 are inadequate incentives or accountabilities in the process, waste and
15 inefficiencies are likely to occur. The standard of “lowest cost” and “lowest
16 storm recovery charges” with accountability compels the transaction parties
17 to achieve the best transaction possible and to avoid a poorly executed,
18 badly priced transaction.

19 Some may argue that an active Commission increases utility legal costs and
20 that this is a reason not to have active Commission and Public Staff
21 involvement in protecting ratepayer interests after a Financing Order has
22 been issued. A review of past legal costs associated with all publicly-offered

1 Ratepayer-Backed Bonds with or without an active commission, Public
2 Staff, or an advisor shows no discernible pattern.

3 **Q. IS THE LENGTH OF TIME IT TAKES TO COMPLETE A**
4 **TRANSACTION A FAIR MEASURE OF SUCCESS IN RATEPAYER-**
5 **BACKED BOND TRANSACTIONS?**

6 A. No. As Public Staff witness Schoenblum testifies, the length of a
7 transaction depends on many factors, such as the speed of the rating
8 agencies' evaluations, efficiency of the underwriters in developing the
9 marketing plan, whether new markets or marketing strategies are being
10 developed, and whether the utility and underwriters work collaboratively
11 with the commission, the ratepayer advocate, and financial advisors in
12 assisting the commission in its oversight function. In some cases,
13 Ratepayer-Backed Bond transactions have been delayed significantly by
14 appeals of the Financing Orders. In other cases, the rating agencies and
15 securities registration processes have been the most time-consuming
16 aspects of a transaction. However, many items can be done concurrently.
17 The best measure of the effectiveness of a transaction is not how fast it is
18 completed, but what the ultimate value for ratepayers.

1 efficient results because each participant pursues its own economic
2 interest, with full knowledge and understanding of the transaction, so that
3 prices are determined through “perfect competition’ based on the free flow
4 of information.

5 However, to create the conditions for “perfect competition,” there needs to
6 be a balance of competing interests in any negotiation. In this transaction
7 as currently proposed by the Companies, the balance is not achieved.
8 Under the procedures proposed by the Joint Petition, the people
9 responsible for repaying the bonds, the ratepayers, are not represented at
10 the negotiating table. They are not protected. Unless the Commission acts
11 to create a process involving Public Staff and the Commission, the results
12 are likely to be skewed against ratepayers’ interests because that’s how the
13 capital markets work. And all top-rated securities, even AAA-rated
14 securities, do NOT price the same; there are differing views. Nothing is
15 automatic except that self-interest rules.

16 As with any publicly-offered securities, the Underwriters will represent their
17 own interests, and the Companies will represent their interests. As
18 discussed in detail in the testimonies of Public Staff witnesses Klein, Moore,
19 Schoenblum, Abramson, Maher and Sutherland, the interests of the
20 Underwriters and the Companies do not necessarily align with the interests
21 of ratepayers, so this lack of representation of ratepayer interests can affect
22 the pricing, the transaction documents and every aspect of the deal.

1 Nothing will occur without the hard work and collaborative efforts of all the
2 parties involved. The Companies, the Public Staff and the Commission can
3 work together, and they can create the balance necessary to manage
4 competition among Underwriters and investors.

5 Public Staff witness Schoenblum describes these best practices in more
6 detail.

7 Effective representation of the interests of ratepayers through Public Staff
8 supporting the Commission at every step through issuance of the bonds is
9 the first element. Decisions affecting ratepayers should be made in
10 consultation with an independent advisor with experience in this unique
11 segment of the capital markets and with a specific and direct fiduciary duty
12 to ratepayers.

13 The second element is the decision-making standard. This is critical. The
14 standard should be the best possible deal for ratepayers at the time of
15 pricing, the lowest possible cost of funds. Anything less, allows for less than
16 optimal results. Why? Very simply, without a lowest cost, best price
17 standard, "why bother?" There is little incentive for any additional effort and
18 hard work. The bonds can be priced quickly and move on.

19 But, the simple facts are that unless you negotiate hard on your behalf with
20 Wall Street, across the table from those sophisticated and large investors
21 with differing views, you will leave substantial amounts of money on the
22 table. Each side is looking out for its own economic interests. The
23 underwriters and investors want the best deal for themselves. One must

1 negotiate equally hard and be equally diligent to arrive at a fair transaction
2 that achieves the lowest cost to ratepayers and is fair value to the investor.
3 So, without a clear standard and a negotiating position that includes the
4 potential for the issuer and ratepayer representatives saying “no” when
5 evaluating offers, Underwriters and investors will have the negotiating
6 leverage to dictate a final cost to ratepayers. Remember, the best way to
7 lose control of the sale price of your house is to tell prospective buyers that
8 you must sell your house today because you really need the money now.
9 Pricing leverage will quickly shift.

10 The final element is for key transaction participants — the Companies,
11 Underwriters, and an independent financial advisor — to deliver to the
12 Commission written certifications, without material qualifications, confirming
13 that what they have done has led to the lowest cost of funds and the lowest
14 storm recovery charges consistent with market conditions at the time of
15 pricing. It is a basic business principle — “put it in writing.”

16 Any prudent person would want it in writing. For example, investors want
17 documentation before they give up their money. They do not rely solely on
18 oral representations before investing. With Sarbanes Oxley and a
19 heightened need to maintain public confidence in business, certifications
20 have become a part of normal business “best practices.”

21 This certification process has been employed successfully in Texas,
22 Florida, West Virginia, Louisiana and New Jersey. Many major

1 Underwriters have delivered these certificates on our transactions, along
2 with all eight utilities. North Carolina ratepayers deserve no less.

3 **Q. PLEASE LIST YOUR RECOMMENDATIONS TO THE**
4 **COMMISSION.**

5 A. I recommend that the Commission:

6 (1) incorporate into its Financing Order the “best practices” as
7 outlined in this testimony;

8 (2) require certifications from the Companies, the bookrunning
9 underwriter(s) and the Public Staff’s financial advisor that the
10 structuring, marketing and pricing of storm recovery bonds in fact
11 achieved the lowest storm recovery charges consistent with market
12 conditions at the time of pricing and the terms of the Financing Order;
13 and

14 (3) approve oversight by the Commission, the Public Staff and its
15 financial advisor through their participation in real-time through a
16 Bond Team on all matters related to the structuring, marketing, and
17 pricing of the storm-recovery bonds.

18 **Q. HOW DO YOU EXPECT THE TRANSACTION TO PROCEED?**

19 A. The Companies, their advisors, as well as the Commission, Public
20 Staff, and their advisors can work collaboratively and expeditiously to
21 complete this important transaction and establish this new financing
22 technique for the benefit of ratepayers and of the Companies.

1 Q. DOES THIS CONCLUDE YOUR TESTIMONY?

2 A. Yes, it does.

1 Q. And, Mr. Fichera, do you have a testimony --
2 I mean, a summary you would like to share with the
3 Commission this morning?

4 A. Yes, I do.

5 Q. Please proceed.

6 A. Good morning. My testimony focuses on the
7 unique situation that the joint petition creates for
8 the Commission to consider. Close to \$1 billion is
9 proposed to be raised, and the natural question for
10 people who will be responsible for paying it back is
11 "at what cost"?

12 The Commission is being asked to use its
13 powerful regulatory authority in ways that have not
14 previously been done in North Carolina. It will create
15 a bond of unusual strength. A completely separate
16 credit from the Companies. The Companies do not pay
17 back the bonds. The ratepayers do directly with an
18 irrevocable charge on their monthly bill. Moreover,
19 this proceeding will establish a template for future
20 issuances of storm recovery bonds, as more damaging
21 hurricanes are expected to occur in North Carolina.

22 In addition to my testimony, the Saber Team
23 is presenting in-depth testimony from top utility and
24 corporate finance executives, a former utility chief

1 executive officer, chief financial officer, and
2 treasurer; a former state utility regulator who oversaw
3 the establishment of another Ratepayer-Backed Bond
4 program, as well as from an independent modeler of
5 Ratepayer-Backed Bonds; and a former utility equity
6 analyst. These people, with decades of experience, all
7 agree that Ratepayer-Backed Bonds are unique and
8 require certain best practices to achieve the lowest
9 cost to the customer transaction.

10 Our experience says that three simple best
11 practices should be followed to achieve the lowest
12 storm recovery charges for ratepayers, and they are,
13 one, ratepayer representation; two, a clear
14 decision-making standard; three, independently verified
15 written certifications.

16 The goal of the financing is for the
17 Commission to get the lowest cost of funds available in
18 the capital markets at the time any storm recovery
19 bonds are priced. Cost matters. If cost did not
20 matter, then the North Carolina Assembly could have
21 allowed the Companies to sell bonds at whatever rate
22 the professional judgement of the underwriters and
23 investors wanted. But the General Assembly did not say
24 that because cost does matter.

1 The capital markets are often thought of as a
2 black box of buyers and sellers rapidly exchanging
3 millions of dollars. They are thought to produce
4 efficient results because each market participant
5 pursues its own economic interest, with full knowledge
6 and understanding of each transaction, so that prices
7 are determined through perfect competition based on a
8 free flow of information. However, my experience is
9 that this is not the case for the capital markets in
10 general or the market for securitized storm recovery
11 bonds in particular.

12 Now, ratepayer Representation. All top-rated
13 securities, even AAA securities, do not price the same.
14 There are differing views. Nothing is automatic in the
15 capital markets except the self-interest rules. The
16 economic interests of the underwriters and the
17 Companies will not necessarily align with the interests
18 of ratepayers. As with publicly-offered securities,
19 the underwriters will represent their own economic
20 interests, and the Companies will represent their own
21 interests. Unless the Commission acts to create a
22 process involving Public Staff and the Commission, the
23 results are likely to be skewed against ratepayer
24 interests. This will affect the pricing, the

1 transaction documents, and every aspect of the deal.

2 Nothing will occur without the hard work and
3 collaborative efforts of all the parties involved. The
4 Companies, the Public Staff, and the Commission can
5 work together. They can create the balance necessary
6 to manage competition among underwriters and investors.
7 Decisions affecting ratepayers should be made in
8 consultation with an independent advisor with
9 experience in this unique segment of the capital
10 markets and with a specific fiduciary duty to
11 ratepayers. Public Staff witness and my colleague
12 Schoenblum describes these best practice in more
13 detail.

14 A Clear Decision Making Standard. This is
15 critical. The standard should be the best possible
16 deal for ratepayers at the time of pricing, the lowest
17 cost of funds that maximizes present value savings to
18 customers. Anything less allows for less-than-optimal
19 results. You might ask why. Well, very simply,
20 without a lowest cost, best price present value
21 standard, there is little incentive for any additional
22 effort and hard work. The bonds can be priced quickly
23 and move on.

24 But the simple facts are that unless a market

1 participant negotiates hard on its own behalf with Wall
2 Street, across the table from those sophisticated and
3 large investors with differing views, that market
4 participant will leave substantial amounts of money on
5 the table. Each side is looking out for its own
6 economic interests. The underwriters and investors
7 want the best deal for themselves. Other market
8 participants must negotiate equally hard and be equally
9 diligent to arrive at a fair transaction that achieves
10 the lowest cost to ratepayers and is fair value to the
11 investor.

12 So without a clear standard and negotiating
13 position that includes the potential for the issuer and
14 ratepayer representatives saying no when evaluating
15 offers, underwriters and investors will have the
16 negotiating leverage to dictate a final cost to
17 ratepayers. Remember, the best way for a homeowner to
18 lose control of the sale of the price of their house is
19 for her to tell prospective buyers that she must sell
20 her house today because she really needs the money now.
21 Pricing leverage will quickly shift.

22 The third and final element of best practices
23 is a basic business principle. Put it in writing.
24 Written certifications. The key transaction

1 participants: the Companies, underwriters, and an
2 independent financial advisor, should deliver to the
3 Commission independent written certifications, without
4 material qualifications, confirming that what they have
5 done has, in fact, led to the lowest cost of funds and
6 the lowest storm recovery charges consistent with
7 market conditions at the time of pricing. With these
8 confirming certifications in hand, the Commission can
9 make the final go/no-go decision.

10 Any prudent person would want it in writing.
11 For example, investors want documentation before they
12 give up their money. They do not rely solely on oral
13 representations before investing. With Sarbanes Oxley
14 and a heightened need to maintain public confidence in
15 business, written certifications have become a part of
16 normal business best practices.

17 These best practices were successfully
18 implemented with Duke Energy for Florida ratepayers on
19 a similar transaction. North Carolina ratepayers
20 deserve no less.

21 This completes my summary. Thank you.

22 Q. Thank you, Mr. Fichera.

23 MR. CREECH: The witness is available
24 for cross examination. We would, however, like to

1 continue on with the presentation of the initial
2 summaries of the panel.

3 MR. GRANTMYRE: The Public -- this is
4 William Grantmyre. The Public Staff's next witness
5 to present the testimony is Brian Maher.

6 DIRECT EXAMINATION BY MR. GRANTMYRE:

7 Q. Mr. Maher, would you please state your name
8 and address? You're muted, I think.

9 A. (Brian Maher) Okay. My name is Brian Maher.
10 My address is 8787 Bay Colony Drive, Naples, Florida.

11 Q. And by whom are you filing testimony?

12 A. I'm filing testimony as a senior advisor of
13 Saber Partners.

14 Q. And they are the financial advisor to the
15 Public Staff?

16 A. Correct.

17 Q. Now, did you prefile in this case direct
18 testimony consisting of 32 pages and four exhibits?

19 A. Yes.

20 Q. And if I were to ask you the same questions
21 again today, would your answers be the same?

22 A. Yes.

23 MR. GRANTMYRE: And, Madam Chair, we
24 would request that his direct testimony be copied

1 into the record as if given orally, and the four
2 exhibits be identified.

3 CHAIR MITCHELL: All right.

4 Mr. Grantmyre, my records indicate that the witness
5 sponsored five exhibits.

6 THE WITNESS: I think that's true. I
7 wasn't going to correct it, but yes, there are five
8 exhibits.

9 CHAIR MITCHELL: Okay. All right.
10 Hearing no objection, then, to your motion,
11 Mr. Grantmyre, the prefilled testimony of witness
12 Maher consisting of 32 pages shall be copied into
13 the record as if delivered orally from the stand.
14 The five exhibits to those -- to that testimony
15 will be identified as they were when prefilled.

16 (Maher Exhibits 1 through 5, were
17 identified as they were marked when
18 prefilled.)

19 (Whereupon, the prefilled direct
20 testimony of Brian Maher was copied into
21 the record as if given orally from the
22 stand.)

23
24

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

Docket No. E-2, Sub 1262

Docket No. E-7, Sub 1243

In the Matter of)	
Joint Petition of Duke Energy Carolinas,	)	TESTIMONY OF
LLC and Duke Energy Progress, LLC	)	BRIAN A. MAHER
Issuance of Storm Recovery Financing	)	SENIOR ADVISOR,
Orders	)	SABER PARTNERS, LLC

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

Docket No. E-2, Sub 1262

Docket No. E-7, Sub 1243

Direct Testimony of

Brian A. Maher Senior Advisor

Saber Partners, LLC

December 21, 2020

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INTRODUCTION

1 **Q. PLEASE STATE YOUR NAME AND ADDRESS.**

2 A. My name is Brian A.Maher. I live at 8787 Bay Colony Drive, Naples,
3 Florida.

4 **Q. WHAT IS YOUR POSITION WITH SABER PARTNERS LLC?**

5 A. I am currently a Senior Advisor to Saber Partners, LLC (Saber
6 Partners or Saber).

7 **Q. WOULD YOU BRIEFLY PROVIDE AN OVERVIEW OF YOUR
8 EDUCATION AND PROFESSIONAL EXPERIENCE?**

9 A. I graduated from Dartmouth College in 1970 Magna Cum Laude with
10 a degree in Romance Languages. In 1973, I received a Master's
11 degree in International Relations with a concentration in International
12 Business and Finance from The Fletcher School of Law and
13 Diplomacy. That year I joined Exxon Corporation (now ExxonMobil
14 Corporation) where I worked for over 33 years, principally in the
15 financial area, until my retirement from the company in 2006.
16 Through multiple assignments in the United States and overseas, I
17 progressed to the senior management level, holding positions of
18 Treasurer for all international operations and Assistant Treasurer of
19 the corporation. For over ten years, part of my responsibilities
20 included supervision of all of ExxonMobil's capital markets activities.
21 During that period I managed billions of dollars of financings and
22 presented annual corporate financing plans and periodic financing

1 performance assessments to the ExxonMobil Management
2 Committee, and at various times to the Board Finance Committee.
3 In addition, during my career I served as president of the
4 corporation's worldwide insurance operations and oversaw
5 worldwide pension and benefits funds, including serving on the
6 New York Stock Exchange Corporate Pension Advisory Committee.

7 **Q. PLEASE STATE YOUR RELATIONSHIP WITH SABER**
8 **PARTNERS.**

9 A. Since 2006, I have been a senior advisor to Saber Partners where I
10 have participated in several of Saber's financial advisory
11 transactions.

12 **Q. WHAT IS THE PURPOSE OF YOUR PRESENTATION TODAY?**

13 A. The purpose of my testimony is to give my perspective on the
14 proposed securitization financing. My main focus will be the
15 appropriate relationship between (i) the North Carolina Utilities
16 Commission (Commission) and the Public Staff and its independent
17 experts and advisors, who I believe are best placed to be the main
18 representatives of the ratepayers' economic interests, and (ii) the
19 other key parties in the transaction, essentially Duke Energy
20 Carolinas, LLC (DEC) and Duke Energy Progress, LLC (DEP and,
21 together with DEC, the Companies), the Companies' advisors, and

1 the investment banks that will likely underwrite the storm recovery
2 bond issue.

3 **RELATIONSHIP BETWEEN UNDERWRITERS, ISSUERS AND**
4 **RATEPAYERS**

5 **Q. FROM YOUR EXPERIENCE, WHAT RELATIONSHIP DO YOU**
6 **EXPECT BETWEEN BOND ISSUERS AND THE BANKS THAT**
7 **SERVE AS UNDERWRITERS IN TYPICAL CORPORATE BOND**
8 **ISSUANCE TRANSACTIONS?**

9 A. As an employee or officer of ExxonMobil, I always expected to
10 develop a cooperative and collegial relationship with the banks that
11 underwrote the bonds to achieve the lowest overall costs possible
12 for the financings. This required a lot of work on both sides. In
13 traditional corporate bond transactions, the issuer bears the full
14 economic burden of repaying the bonds. Banks that underwrite the
15 bonds bear none of the economic burdens of repaying the bonds.
16 Consequently, issuers of bonds and the banks that underwrite the
17 bonds share some, but not all, of the same key objectives for the
18 transaction. On the positive side, the banks very much want to be
19 perceived as capable of executing an efficient, competitive
20 transaction to earn repeat business as well as new business from
21 other issuers that monitor the market. But issuers and banks are
22 often on opposite sides of the table when it comes to (i) profits to be
23 earned by the banks, (ii) the amount of effort and time the banks

1 need to spend to achieve the best possible transaction, and (iii) the
2 desire of the banks' investor clients to earn attractive returns. For
3 these reasons, issuers should always play an active role in the
4 transaction to make sure their own interests are maximized as
5 opposed to remaining passive and depending too heavily on their
6 banks for market information, investor outreach, or other aspects of
7 the financing. It is essential to keep in mind at all times that the
8 underwriting banks are sophisticated and operate in furtherance of
9 their own financial interests. Issuers must do the same.

10 **Q. WHAT RELATIONSHIP DO YOU EXPECT BETWEEN ISSUERS**
11 **OF TRADITIONAL CORPORATE BONDS AND BANKS THAT**
12 **SERVE AS FINANCIAL ADVISORS TO THOSE BOND ISSUERS?**

13 A. I would expect their interests to be perfectly aligned. ExxonMobil
14 employs an experienced staff of professionals with deep experience
15 in issuing traditional corporate bonds. Consequently, ExxonMobil
16 generally did not hire outside financial advisors in connection with its
17 traditional bond issuance transactions. But when a financial
18 transaction involved unusual features, ExxonMobil would sometimes
19 hire an investment bank to serve as financial advisor for that
20 transaction. In those transactions, I expected the interests of
21 ExxonMobil's financial advisor to be perfectly aligned with the
22 interests of ExxonMobil.

1 price for gains on the first day of trading. After the 2005 final appellate
2 court decision in this aspect of the eToys litigation, it became
3 universal practice for underwriting agreements to expressly disclaim
4 any fiduciary relationship with the issuer of securities. See Hunton
5 & Williams, "Client Update – When Does an Underwriter Owe a
6 Fiduciary Duty to an Issuer," dated August 2005, attached to my
7 testimony as Maher Exhibit 3.

8 **Q. AS STRUCTURING ADVISORS TO THE COMPANIES, DO**
9 **GUGGENHEIM SECURITIES AND ATKINS CAPITAL HAVE A**
10 **FIDUCIARY RELATIONSHIP?**

11 A. Apparently not. In responding to PS DR 2-2(g), Witness Heath
12 states: "The engagement letters between DEC and DEP and
13 Guggenheim Securities and Atkins Capital do not create any
14 fiduciary relationships between the parties. This is common practice
15 for advisory services engagements."

16 **Q. WHAT ARE THE IMPORTANT ISSUES FOR THE COMMISSION**
17 **TO KNOW ABOUT FIDUCIARY RELATIONSHIPS?**

18 A. In broad terms, a service provider that has a fiduciary responsibility
19 to its client commits to act in the client's best interests to the
20 exclusion of any contrary interests. Where a fiduciary relationship
21 exists, the client should be comfortable that the service provider is
22 looking out for the client's best interests. As I will describe, that alone

1 does not ensure the best result for a given financial transaction. Even
2 where there is a fiduciary relationship, sophisticated clients should
3 work actively with their service providers to ensure alignment is
4 complete in all important aspects of the transaction. Where a
5 fiduciary relationship does not exist, it is extremely important for the
6 client to stay actively involved because the service provider could be
7 subject to motivations in some way contrary to the best interests of
8 the client.

9 There is much debate about when a “fiduciary relationship” arises
10 between parties to commercial contracts. A 2006 speech by Lori A.
11 Richards, Director, Office of Compliance Inspections and
12 Examinations, U.S. Securities and Exchange Commission (SEC),
13 titled “Fiduciary Duty: Return to First Principles” described it this
14 way:

15 Many different types of professions owe a fiduciary
16 duty to someone — for example, lawyers to their
17 clients, trustees to beneficiaries, and corporate officers
18 to shareholders. Fiduciary duty is the *first principle* of
19 the investment adviser — because the duty comes not
20 from the SEC or another regulator, but from common
21 law. Some people think “fiduciary” is a vague word
22 that’s hard to define, but it’s really not difficult to define
23 or to understand. Fiduciary comes from the Latin word
24 for “trust.” A fiduciary must act for the benefit of the
25 person to whom he owes fiduciary duties, to the
26 exclusion of any contrary interest.¹

¹ Eighth Annual Investment Adviser Compliance Summit, Washington, D.C., February 27, 2006; <https://www.sec.gov/news/speech/spch022706lar.htm>.

1 The Securities Industry Markets Association (SIFMA), which is the
2 broker-dealer's chief lobbying firm, defined on their website "fiduciary
3 relationship" and "fiduciary duty" in this way as further described in
4 Maher Exhibit 4:

5 "A fiduciary relationship is generally viewed as the
6 highest standard of customer care available under
7 law. Fiduciary duty includes both a duty of care and a
8 duty of loyalty. Collectively, and generally speaking,
9 these duties require a fiduciary to act in the best
10 interest of the customer, and to provide full and fair
11 disclosure of material facts and conflicts of interest."

12 **Q. HAVE THERE BEEN DEVELOPMENTS IN THIS AREA?**

13 A. Yes. News reports on the financial markets have reported on initial
14 public offerings in the stock market. Commissioners may be aware
15 of stories where a stock is priced in a public offering, and then is
16 immediately re-sold at a higher price, as in the case of eToys
17 mentioned above. In 1999, eToys issued stock in an initial public
18 offering. Goldman Sachs & Co. served as the lead managing
19 underwriter for this initial public offering. The stock quadrupled when
20 it began trading, but two years later eToys was in bankruptcy. Its
21 creditors (including bondholders) filed a complaint in New York state
22 court alleging

1 “an advisory relationship that was independent of the
2 underwriting agreement. Specifically, plaintiff alleges
3 eToys was induced to and did repose confidence in
4 Goldman Sachs' knowledge and expertise to advise it
5 as to a fair IPO price and engage in honest dealings
6 with eToys' best interest in mind. Essentially, according
7 to the complaint, eToys hired Goldman Sachs to give it
8 advice for the benefit of the company, and Goldman
9 Sachs thereby had a fiduciary obligation to disclose
10 any conflict of interest concerning the pricing of the
11 IPO. Goldman Sachs breached this duty by allegedly
12 concealing from eToys its divided loyalty arising from
13 its profit-sharing arrangements with clients.”²

14 The trial court and an intermediate appellate court declined to
15 dismiss this aspect of the complaint, opining that the breach of
16 fiduciary duty claim was correctly sustained upon allegations
17 showing a preexisting relationship between eToys and Goldman
18 Sachs that justified eToys' alleged trust in pricing the shares. In EBC
19 I, Inc. v. Goldman, Sachs & Co., 5 N.Y.3d 11 (N.Y. 2005), 799
20 N.Y.S.2d 170, 832 N.E.2d 26 (2005), the Court of Appeals of the
21 State of New York also declined to dismiss this aspect of the
22 complaint and remanded this aspect of the case to the lower courts
23 for further proceedings, stating: “Accepting the complaint's
24 allegations as true, as the Court must at this stage, plaintiff has
25 sufficiently stated a claim for breach of fiduciary duty.”

26 This led to express disclaimers of any fiduciary duty in underwriting
27 agreements as well as in agreements for structuring advisory

² EBC I, Inc. v. Goldman, Sachs & Co., 5 N.Y.3d 11 (N.Y. 2005), 799 N.Y.S.2d 170, 832 N.E.2d 26 (2005).

1 services. The practice of explicit disclosures disavowing any
2 fiduciary relationship continues to this day.

3 **Q. ARE YOU GIVING AN OPINION AS TO WHETHER THERE IS A**
4 **LEGAL REQUIREMENT OF ANY PARTY IN THIS TRANSACTION**
5 **TO HAVE A FIDUCIARY RELATIONSHIP?**

6 A. No. I am discussing the important issues related to whether a
7 fiduciary relationship exists and what the Commission should
8 consider in deciding how to evaluate information it receives from
9 different parties to the proposed transaction.

10 **Q. DO UNDERWRITERS HAVE A FIDUCIARY RELATIONSHIP WITH**
11 **AN ISSUER OF SECURITIES?**

12 A. In my experience, underwriters claim they have no fiduciary
13 relationship to issuers. Underwriting agreements prepared by
14 counsel for the underwriters now include a specific declaration that
15 the underwriters have no fiduciary relationship with the issuer.
16 Issuers frequently are asked to acknowledge this affirmatively in the
17 underwriting agreement. For example, the Underwriting Agreement
18 filed with the Securities and Exchange Commission for the 2016
19 Duke Energy Florida, LLC, securitization transaction states:

20 16. No Advisory or Fiduciary Relationship. Each of the
21 Issuer and the Depositor acknowledges and agrees
22 that (a) the purchase and sale of the Bonds pursuant
23 to this Agreement, including the determination of the
24 offering price of the Bonds and any related discounts
25 and commissions, is an arm's-length commercial

1 transaction between the Issuer and the Depositor, on
 2 the one hand, and the several Underwriters, on the
 3 other hand, (b) in connection with the offering and the
 4 process leading thereto, each Underwriter is and has
 5 been acting solely as a principal and is not the agent or
 6 fiduciary of either the Issuer or the Depositor, any of
 7 their subsidiaries or their respective members,
 8 directors, creditors, employees or any other party,
 9 (c) no Underwriter has assumed or will assume an
 10 advisory or fiduciary responsibility in favor of the Issuer
 11 or the Depositor with respect to the offering or the
 12 process leading thereto (irrespective of whether such
 13 Underwriter has advised or is currently advising the
 14 Issuer or the Depositor or any of its subsidiaries on
 15 other matters) and no Underwriter has any obligation
 16 to the Issuer or the Depositor with respect to the
 17 offering except the obligations expressly set forth in
 18 this Agreement, (d) the Underwriters and their
 19 respective affiliates may be engaged in a broad range
 20 of transactions that involve interests that differ from
 21 those of the Issuer or the Depositor, (e) any duties and
 22 obligations that the Underwriters may have to the
 23 Issuer or the Depositor shall be limited to those duties
 24 and obligations specifically stated herein and (f) the
 25 Underwriters have not provided any legal, accounting,
 26 regulatory or tax advice with respect to the offering and
 27 each of the Issuer and the Depositor has consulted its
 28 own respective legal, accounting, regulatory and tax
 29 advisors to the extent it deemed appropriate.³

30 **IMPORTANCE OF FIDUCIARY-BEST INTERESTS OF**
 31 **RATEPAYER RELATIONSHIP**

32 **Q. WHY IS THIS IMPORTANT?**

33 A. Bond underwriters will typically propose an offering process,
 34 including bond pricing, whereby the underwriters use their

³ Duke Energy Florida Project Finance, LLC \$1,294,290,000 Series A Senior Secured Bonds Underwriting Agreement,
https://www.sec.gov/Archives/edgar/data/37637/000110465916128039/a16-2779_13ex1d1.htm.

1 “professional judgment” in establishing price guidance and change
2 that price guidance “solely in their professional judgment.” This is
3 what the Companies’ witness Atkins has testified. However, as
4 clearly stated in the above excerpt from an underwriting agreement
5 involving Morgan Stanley, the underwriters act for their own benefit
6 and cannot always be counted on to act solely on behalf of the
7 Issuer. Pricing is arguably the most important component of offering
8 securities in the market. I believe this is a compelling reason why
9 bond issuers need to be very active in the offering process: to protect
10 their own interests.

11 **Q. IS THIS LANGUAGE FOUND ONLY IN THE INVESTOR-OWNED**
12 **RATEPAYER-BACKED BOND TRANSACTION YOU CITED?**

13 A. No. I have reviewed a survey of all investor-owned utility
14 securitization filings from 2004 to present. As noted above, beginning
15 in 2005, a new section appeared in these agreements. Each form of
16 underwriting agreement had the exact same or similar language. The
17 survey is attached to my testimony as Maher Exhibit 1.

18 **Q. IS THIS, OR SIMILAR LANGUAGE CONTAINED IN THE**
19 **UNDERWRITING AGREEMENT BETWEEN THE COMPANIES**
20 **AND THE UNDERWRITERS TO BE ENTERED IN THIS**
21 **TRANSACTION?**

1 A. Yes, it likely will be. In response to data request questions inquiring
2 if underwriters of securities have a duty to the issuer of those
3 securities and is it a fiduciary duty the Companies' witness Heath
4 stated that the underwriters do not have a fiduciary duty to the issuer.

5 **Q. DO FINANCIAL ADVISORS TO ISSUERS HAVE A FIDUCIARY**
6 **RELATIONSHIP WITH THE ISSUER?**

7 A. Not necessarily. One has to review the specific contract with the
8 advisor and what the duties of the financial advisor are under state
9 and federal laws. Many times, as a condition of hiring them, financial
10 advisors require the issuer to waive any assertion of a fiduciary
11 relationship. As mentioned above, in responding to PS DR 2-2(g),
12 Witness Heath acknowledges that the engagement letters between
13 the Companies and Guggenheim Securities and Atkins Capital do
14 not create a fiduciary relationship between the parties.

15 Moreover, financial advisors often require full and complete
16 indemnification from anything arising out of their advice. These
17 indemnifications are often long legal documents. The basic rule in
18 negotiating financial advisor contracts should be Caveat Emptor or
19 "buyer beware."

20 Guggenheim's and Atkins Capital's Engagement Letters with the
21 Companies include a two-page Appendix titled "Indemnification
22 Provisions." It is very difficult for the layman to read, and its length

1 and complexity underscore for the Commission how important a topic
2 this is to the financial community. Among other things in the lengthy
3 document, it states:

4 Each of DEC and DEP hereby jointly and severally
5 agrees to (a) indemnify and hold harmless
6 Guggenheim Securities, to the fullest extent permitted
7 by law, from and against any and all losses, claims,
8 damages, obligations, penalties, judgments, awards
9 and other liabilities (whether direct, joint and several or
10 otherwise) as and when incurred by Guggenheim
11 Securities (collectively, "Liabilities") and (b) fully
12 reimburse Guggenheim Securities for any and all fees,
13 costs, expenses and disbursements (in all such cases,
14 whether legal or otherwise) as and when incurred by
15 Guggenheim Securities (collectively, "Expenses"),
16 including those of investigating, preparing for
17 (including, without limitation, preparing, reviewing or
18 furnishing documents), participating in, defending
19 against or giving testimony with respect to any private,
20 regulatory, self-regulatory or governmental requests,
21 inquiries, investigations, actions, claims,
22 interrogatories, subpoenas, suits, litigation,
23 proceedings or injunctions, whether or not in
24 connection with any threatened or actual litigation,
25 arbitration or other dispute resolution process and
26 whether or not Guggenheim Securities is a direct party
27 thereto (collectively, "Actions"), in the case of each of
28 the foregoing clauses (a) and (b) whether directly or
29 indirectly caused by, relating to, based upon, arising
30 out of or in connection with any of the following: (i) any
31 advice or services requested of, or rendered or to be
32 rendered by, Guggenheim Securities pursuant to the
33 Agreement, (ii) any actions or inactions by
34 Guggenheim Securities with respect to the Agreement,
35 (iii) any transaction or financing in connection with or
36 related to the Agreement or (iv) the determination and
37 enforcement by Guggenheim Securities of its rights
38 pursuant to the Agreement (including, without
39 limitation, these Indemnification Provisions); provided,
40 however, such indemnification agreement will not
41 apply to any portion of any such Liability or Expense to
42 the extent it is found in a final judgment by a court of

1 competent jurisdiction (not subject to further appeal) to
2 have resulted primarily and directly from the gross
3 negligence or willful misconduct of Guggenheim
4 Securities.

5 **Q. DOES SABER PARTNERS HAVE A SIMILAR INDEMNIFICATION**
6 **AGREEMENT WITH PUBLIC STAFF?**

7 A. No, it does not.

8 **Q. DOES SABER PARTNERS HAVE A FIDUCIARY DUTY TO**
9 **NORTH CAROLINA RATEPAYERS?**

10 A. Yes. As financial advisor to the Public Staff, Saber Partners
11 considers itself as having a fiduciary duty to North Carolina
12 ratepayers.

13 **Q. IS THERE ANY DIFFERENCE IF THE FINANCIAL ADVISOR IS AN**
14 **ADVISOR TO A STATE OR LOCAL GOVERNMENT OR NOT-**
15 **FOR-PROFIT INSTITUTION INSTEAD OF AN INVESTOR-OWNED**
16 **UTILITY OR ONE OF ITS SUBSIDIARIES?**

17 A. Yes. As a result of the financial crisis of 2008, Congress enacted
18 comprehensive financial reform commonly known as the Dodd-Frank
19 Act. One of the requirements of the Dodd-Frank Act was to impose
20 a federal fiduciary duty on all advisors to state and local governments
21 and on not-for-profit institutions that issue bonds in the municipal
22 bond market.

1 **Q. DOES THIS REQUIREMENT APPLY TO THE CORPORATE**
2 **BOND MARKET?**

3 A. No, it is not a federal mandate in the corporate bond market.
4 However, the fact that the subject of fiduciary responsibility has
5 become a public policy issue highlights its importance for corporate
6 issuers as well and should be a guide to the Commission in
7 connection with securitized storm recovery bonds where the
8 sponsoring utilities have no financial obligation to repay those bonds.

9 **Q. WHO WOULD ISSUE THE SECURITIZATION BONDS**
10 **PROPOSED BY THE COMPANIES?**

11 A. The Companies each propose to form a wholly owned, special
12 purpose entity (SPE) to issue storm recovery bonds.

13 **Q. WILL EITHER THE COMPANIES OR THE SPECIAL PURPOSE**
14 **ENTITY TO BE CREATED TO ISSUE THE BONDS HAVE THE**
15 **SAME FINANCIAL INCENTIVES TO ACHIEVE THE LOWEST**
16 **OVERALL COST OF FUNDS AS DO MORE TRADITIONAL**
17 **ISSUERS OF CORPORATE DEBT SECURITIES?**

18 A. No. The securitization transaction is different from normal corporate
19 debt issues in which the issuer has a direct interest in minimizing the
20 cost of the transaction in order to maximize economics for its
21 shareholders. For traditional utility debt issues, as well, incentives
22 exist to minimize the costs of the transaction. Here the Companies

1 propose that the storm recovery bonds will be issued by SPEs. This
2 is simply a mechanism to facilitate the transfer of funds from the
3 ratepayers to the Companies, while the ratepayers alone will
4 ultimately bear all transaction costs and all costs of repaying the
5 storm recovery bonds. The Companies will receive net proceeds of
6 the bonds to recover previously incurred costs. While I do not doubt
7 that the Companies would desire that its ratepayers incur low storm
8 recovery charges, the Companies' main motivation is to receive the
9 debt proceeds in a timely, efficient manner. Therefore, the
10 Companies do not share the same incentives to achieve the lowest
11 overall cost of funds. This is really just a matter of common sense
12 and human nature. If I were going to borrow money and someone
13 else agreed to repay it for me, then I would not be as concerned
14 about the interest rate and other terms of the loan as I would be if I
15 were on the hook to repay the loan myself. Therefore, it is left to the
16 Commission and the Public Staff to ensure that the ratepayers
17 achieve the lowest overall cost of funds for the bonds and the lowest
18 storm recovery charges consistent with market conditions at the time
19 the bonds are priced. Under the Companies' current proposal, in my
20 opinion, ratepayer interests would not be maximized at the
21 negotiating table. In other jurisdictions, the independent financial
22 advisor to the commission has the responsibility, along with the

1 commission and the commission staff, to help make that happen.
2 This is what I propose should happen here.

3 **WAYS TO PROTECT RATEPAYERS INTERST BY MODIFYING**
4 **THE COMPANIES' PROPOSAL**

5 **Q. CAN YOU EXPAND ON YOUR OPINION THAT RATEPAYER**
6 **INTERESTS WOULD NOT BE MAXIMIZED UNDER THE**
7 **COMPANIES' PROPOSAL?**

8 A. I believe that the Companies' proposal would rely too heavily on the
9 Companies, their advisors and the underwriters, none of which has
10 a fiduciary responsibility to the Commission or the ratepayers in the
11 proposed storm recovery bond transaction. As I said above, I do not
12 doubt that the Companies have an interest in achieving low storm
13 recovery charges for the ratepayer, but the Companies do not share
14 the same incentives to achieve the lowest storm recovery charges.

15 **Q. IN A BROAD SENSE, HOW CAN THE COMMISSION, THE**
16 **PUBLIC STAFF AND THEIR INDEPENDENT FINANCIAL**
17 **ADVISOR(S) SUCCESSFULLY ACHIEVE THE OBJECTIVE OF**
18 **ENSURING THAT RATEPAYER INTERESTS ARE EFFECTIVELY**
19 **MAXIMIZED WITH RESPECT TO THIS TRANSACTION?**

20 A. The Commission, the Public Staff and their independent financial
21 advisor(s) need to be fully involved in working in a cooperative way
22 with the Companies and the Companies' advisor to achieve that

1 objective. That will require optimal structuring of the storm recovery
2 bond issue, which includes:

3 (a) ensuring that disclosure documents and marketing materials
4 accurately reflect the superior credit and minimal risks of
5 storm recovery bonds;

6 (b) selecting the bank(s) to be used as underwriters and defining
7 the role the banks will play and fees the banks will earn;

8 (c) actively monitoring the market to choose the most
9 advantageous timing of the transaction;

10 (d) developing independent pricing expectations;

11 (e) participating in execution of the transaction to ensure that the
12 size of the investor population is maximized and that the
13 investor population is thoroughly educated about the
14 extremely high credit quality of the storm recovery bonds; and

15 (f) at the time of pricing of the bonds, ensuring that the
16 Commission, the Public Staff and their financial advisor(s)
17 monitor and provide input to the pricing process so that the
18 lowest storm recovery charge is achieved.

19 As part of the process, the bookrunning underwriter(s) should
20 commit, in writing, to achieving the lowest storm recovery bond
21 charge for the ratepayers, and the bookrunning underwriter(s) should

1 certify after pricing that they have done so. (For an example, see
2 Public Staff witness Klein's Exhibit 4.)

3 There are many examples in the financial world where written
4 certifications have become the standard. When a person is required
5 to pledge something in writing, rather than just orally, and has to
6 account for results later, that person is more likely to take that pledge
7 seriously. Public Staff witness Sutherland's testimony provides a
8 more granular description of the "Best Practices" that I believe should
9 be employed to achieve a lowest storm recovery charge financing.
10 His testimony, along with that of Public Staff witness Schoenblum,
11 documents the savings that have been achieved in previous
12 Ratepayer-Backed Bond transactions when an active and
13 independent financial advisor has been involved and when that
14 active and independent financial advisor has employed the above
15 approach.

16 **ACHIEVING THE LOWEST COST TO RATEPAYERS**

17 **Q. HOW IS IT REALLY POSSIBLE TO KNOW IN ABSOLUTE TERMS**
18 **THAT THE LOWEST STORM RECOVERY BOND CHARGE**
19 **TRANSACTION HAS BEEN ACHIEVED?**

20 **A.** When issuers or regulators ask underwriters for such a certificate or
21 certification as referenced above, they are really asking underwriters
22 to confirm in writing that all actions the underwriters believe would

1 minimize the overall cost of the financing have in fact been taken. In
2 practice, that confirming certificate should be supported by
3 corroborating data, such as how the actual pricing compared to the
4 expectations developed by the underwriters, as well as expectations
5 developed independently by the issuer(s), how actual pricing
6 compared to secondary market pricing of other similar securities at
7 the time of pricing, and how successful the iterative price talk process
8 was in lowering the interest rate to the optimal point of balancing
9 investor demand with the supply of storm recovery bonds being
10 offered.

11 **Q. SHOULD THE LOWEST STORM RECOVERY CHARGE**
12 **STANDARD APPLY TO ALL COSTS ASSOCIATED WITH THE**
13 **TRANSACTION?**

14 A. Yes. However, in considering how the lowest storm recovery charge
15 standard should be applied, there is a difference between buying
16 services and agreeing to pay interest. Services should not be
17 determined solely on the basis of a dollar cost, but also the quality of
18 the services, with the goal of obtaining the best overall value. In
19 contrast, when an issuer borrows money there is no reason to agree
20 to pay more interest (in present value terms) than is absolutely
21 necessary. It is only logical that this should be the decision-making
22 standard for pricing a borrowing. Without such a standard, a bond

1 issuer might save a lot of time and effort by just accepting whatever
2 interest rate the underwriters and investors want.

3 **ALL AAA-RATED SECURITIES DO NOT PRICE ALIKE**

4 **Q. IF THE STORM RECOVERY BONDS ARE RATED “AAA,” DOES**
5 **THAT NOT ENSURE THAT THE LOWEST OVERALL COSTS AND**
6 **THE LOWEST STORM RECOVERY CHARGES WILL BE**
7 **ACHIEVED?**

8 A. Unfortunately not. In my many years overseeing ExxonMobil's
9 capital markets activities, I learned that bond issues could almost
10 always be done at lower rates than the best market preliminary
11 indications given by the banks. This was true despite the fact that
12 ExxonMobil was a well-known and coveted “AAA”-rated debt issuer.
13 Active involvement by ExxonMobil to create competition among the
14 banks and to demand the best execution consistently added value.

15 It is also true that all “AAA” debt is not viewed alike by investors in
16 the debt capital markets. For example, when I worked at ExxonMobil,
17 “AAA”-rated ExxonMobil or Federal Agency credits would command
18 better pricing than most “AAA”-rated structured debt securities which
19 were backed solely by a pool of intangible contract rights such as
20 mortgages or credit card receivables.

1 **Q. ARE THE STORM RECOVERY BONDS PROPOSED TO BE**
2 **ISSUED IN THIS CASE LIKELY TO PERFORM STRONGLY IN**
3 **THE “AAA” MARKET?**

4 A. Yes. In my view, the proposed bonds are likely to achieve a very
5 strong “AAA” performance because they will be backed by a state
6 regulatory guarantee to irrevocably provide for the timely payment of
7 principal and interest from the revenues of an essential service (i.e.,
8 electricity). However, even though there is a fairly long history of this
9 type of utility securitization transaction, the features of these
10 proposed storm recovery bonds are sufficiently complex that I
11 believe an intensive investor education effort and an aggressive
12 marketing process are warranted to ensure that the bonds achieve
13 the tight pricing they deserve.

14 **Q. ARE THERE ANY EXAMPLES OF WAYS AN ISSUER COULD**
15 **ASSIST IN CAPTURING THE FULL VALUE OF THE SECURITIES**
16 **TO BE OFFERED HERE?**

17 A. Yes. The SEC registration statements pursuant to which a number
18 of prior Ratepayer-Backed Bonds have been offered have provided
19 detail about the unusual and superior credit quality of the securities.
20 The SEC materials are the primary way of informing investors of the
21 benefits and risks of the securities in a fair and balanced manner. For
22 example, the final prospectuses included in SEC registration
23 statements for investor-owned utility securitized bonds issued in

1 2007 and 2009 for the benefit of Monongahela Power Company and
2 for The Potomac Edison Company include the following language:

3 Credit Risk: PSC-Guaranteed True-Up Mechanism
4 and State Pledge Will Limit Credit Risk. In the
5 Financing Act, the State of West Virginia pledges to
6 and agrees with the bondholders, any assignee and
7 any financing parties that the state will not take or
8 permit any action that impairs the value of
9 environmental control property or, except as part of the
10 true-up process, reduce, alter or impair environmental
11 control charges that are imposed, collected and
12 remitted for the benefit of the bondholders, any
13 assignee, and any financing parties, until any principal,
14 interest and redemption premium in respect of
15 environmental control bonds, all financing costs and all
16 amounts to be paid to an assignee or financing party
17 under an ancillary agreement are paid or performed in
18 full.⁴

19 The broad-based nature of the true-up mechanism and the State
20 Pledge serve to effectively eliminate, for all practical purposes and
21 circumstances, any credit risk to the payment of the bonds (i.e., that
22 sufficient funds will be available and paid to discharge the principal
23 and interest of each issue of bonds when due).

24 The kind of language used in the above example is stronger than
25 that which has been used in some other securitizations and can be
26 helpful to achieve the financial benefits of the superior credit
27 characteristics of the proposed storm recovery bonds.

⁴ <https://www.sec.gov/Archives/edgar/data/1384732/000095012007000242/mp-prospectus.htm> (at page 26);
<https://www.sec.gov/Archives/edgar/data/1384731/000095012007000244/pe-prospectus.htm> (at page 26);
<https://www.sec.gov/Archives/edgar/data/1384732/000119312509255754/d424b1.htm> (at page 27);
<https://www.sec.gov/Archives/edgar/data/1384731/000119312509255755/d424b1.htm> (at page 28).

1 **Q. WAS THIS DISCLOSURE LANGUAGE CONCERNING THE**
2 **“CREDIT RISK” OF RATEPAYER-BACKED BONDS**
3 **DEVELOPED THROUGH A COLLABORATIVE AND COLLEGIAL**
4 **PROCESS WITH THE UTILITY?**

5 A. Yes. Saber’s records have been shared with me concerning this
6 disclosure language. I have reviewed those records and have found
7 they indicate that this “credit risk” language was developed for an
8 earlier Ratepayer-Backed Bond in Texas for Oncor/TXU where
9 Saber served as the independent financial advisor to the Public Utility
10 Commission of Texas in a similar capacity that we propose here.
11 Saber’s records show that this disclosure language was proposed by
12 Hunton & Williams, legal counsel to the investor-owned utility in
13 collaboration and discussion with the independent advisor so as to
14 best inform investors of the unique credit qualities of that utility
15 securitization. (See Maher Exhibit 2)

16 **NEED FOR INDEPENDENT EXPERTISE SUPPORTING**
17 **DESIGNATED COMMISSIONER INVOLVEMENT IN BOND TEAM**

18 **Q. WOULD THE PROPOSED BOND TEAM PLAY THE ROLE YOU**
19 **ARE ADVOCATING SO THAT RATEPAYERS ARE ASSURED**
20 **THE LOWEST STORM RECOVERY CHARGE?**

21 A. That should be the case. However, it all depends on who is on the
22 Bond Team and how the role of the Bond Team is defined and
23 executed. I believe that the Bond Team should consist of the

1 Companies, the Companies' advisor (provided such advisor is not
2 one of the banks acting as underwriter for the transaction), the
3 Commission, either directly or through a designated staff member(s),
4 the Public Staff, and the independent advisors and counsel.

5 I believe it is very important for the lead Commission representative
6 to be closely involved in the project. There are many complexities
7 and this is probably not the type of work that Commissioners
8 undertake on a regular basis. At ExxonMobil our CEO was well
9 versed in every aspect of the business, and when briefed on complex
10 financial matters, could rapidly come up to speed and make informed
11 decisions. In the case of securitization financing, the Commission's
12 lead decision-maker might value more ongoing involvement with
13 Public Staff and their professional advisors to be comfortable that
14 his/her decisions are in the best interests of the ratepayer. It is
15 important that the Bond Team operate independently and entirely in
16 the interest of the ratepayers and not include any of the underwriting
17 banks due to their inherent conflict of interest discussed above. All
18 members of the Bond Team should have a fiduciary relationship with
19 either the Companies, the Commission, or the Public Staff. Decisions
20 of the Bond Team should be a shared responsibility of its members,
21 with the Commission's representatives in a position to make the final
22 decision on a timely basis, often in real time, in the event of any
23 disagreements among Bond Team members. The Bond Team

1 should rigorously follow the market and provide strong input to the
2 underwriters with regard to bond structure, timing of the issue, the
3 education of target investors and the pricing process. After the storm
4 recovery bonds are sold, the Bond Team should follow the trading of
5 the bonds in the secondary market and thoroughly evaluate the
6 execution of the transaction to be comfortable that the best results
7 were in fact obtained for ratepayers, and to learn any lessons for
8 future storm recovery bond issues.

9 **Q. IS IT CLEAR AT THIS POINT IN THE PROCESS HOW THE**
10 **STORM RECOVERY BOND ISSUE SHOULD BE STRUCTURED?**

11 A. Not at this point. We know that the storm recovery bonds will be sold
12 some time in 2021. However, many important details will be
13 determined as the sale date approaches and the market continues
14 to develop. For example, the Companies' financial advisors propose
15 Guggenheim / Atkins to offer both DEC bonds and DEP bonds to
16 investors jointly through an offering of combined storm recovery
17 bonds called "SRB Securities" issued by a grantor trust owned by
18 Duke Energy Corporation. This is such a novel structure that out of
19 the 66 Ratepayer-Backed Bond offerings since 1997, only two
20 transactions used this structure. It must be carefully evaluated.

21 In addition, the exact timing of the bond issue should be flexible and
22 responsive to market conditions. There also should be flexibility in

1 deciding whether to offer and sell all the authorized bonds at the
2 same time, as a single series, or to offer and sell the authorized
3 bonds at different times, as more than one series. Another example
4 is the possible desire for flexibility in breaking a series of bonds into
5 different segments, often referred to as tranches, designed to appeal
6 to different investor bases at the time of sale; e.g., 10-15 year and 2-
7 5 year weighted average life tranches or longer maturities.

8 The pandemic has created unusual market conditions. While
9 benchmark US Treasury rates have fallen to unprecedented lows,
10 the credit spread above these low rates required by investors has
11 been volatile. There are large disparities among credits. The current
12 evolving conditions are not “normal market conditions” that have
13 modest changes over time.

14 **Q. DO YOU HAVE AN OPINION AS TO WHETHER THE STORM**
15 **RECOVERY BOND ISSUE SHOULD BE EXECUTED ON A**
16 **COMPETITIVE OR NEGOTIATED BASIS?**

17 A. Yes, although I think a final decision should be made closer to the
18 time that the bonds could be offered for sale to investors. Regarding
19 the role the underwriters will play, this transaction probably is not
20 ideal for a rigid competitive approach where the issue date is set in
21 advance and the qualifying banks bid on pricing close to that date.
22 This is because, in addition to wanting to remain flexible on timing of

1 the issue, a longer marketing period is warranted to effectively sell
2 the credit to investors. A negotiated approach appears preferable,
3 where a highly competitive process is used to select one or more
4 highly qualified banks to lead the transaction. In a negotiated sale,
5 there are a variety of techniques that can be used to induce the
6 selected underwriters to compete on final pricing. In the end, if the
7 marketing of the bonds is effective, I believe there should be a lot of
8 strong orders from a broad cross section of institutional and retail
9 investors, both from the U.S. domestic and international markets,
10 seeking safety and security to purchase storm recovery bonds from
11 the selected underwriters. Then it is crucial that the market price talk
12 (the indications made to investors about what the possible interest
13 rate will be before actual pricing) be conducted in a manner so that
14 demand and supply are matched at the lowest interest rate possible.
15 As I have said previously, these are areas where a well-informed,
16 aggressive Bond Team can add significant value.

17 **Q. PLEASE SUMMARIZE YOUR TESTIMONY.**

18 A. The proposed storm recovery bonds should achieve a “AAA” rating
19 and perform well in the market. **But superior performance is not**
20 **automatic since all “AAA” bonds do not trade alike.** The key
21 takeaway should be that, while factors such as underwriters’
22 professional opinions are valuable, underwriters do not have any
23 fiduciary responsibility to the ratepayer. Similarly, the Companies’

1 primary responsibility is to their own shareholders. Therefore, the
2 Commission, the Public Staff and their independent financial
3 advisor(s) are in the primary position of having to look out for the
4 ratepayers' best interests. It is critical that they play an active role in
5 all aspects of the transaction. They must be willing to invest all the
6 time necessary in the structuring and take an aggressive stance
7 during the marketing process to capture the lowest cost of financing
8 and the lowest storm recovery charges for the ratepayers. This
9 should involve full participation in the transaction with the Companies
10 and the bond underwriters and, if required, timely decision making
11 by the Commission to resolve any potential financing issues in the
12 ratepayers' best interests.

13 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

14 **A. Yes.**

1 Q. Thank you. Do you have a summary of your
2 testimony, Mr. Maher?

3 A. Yes, I do.

4 Q. Can you please read your summary.

5 A. Yes. My main focus will be the appropriate
6 relationship between; one, the North Carolina Utilities
7 Commission and the Public Staff and its independent
8 experts and advisors, who I believe are best placed to
9 be the main representatives of the ratepayers' economic
10 interests; and two, the other key parties in the
11 transaction, essentially Duke Energy Carolinas, LLC,
12 Duke Energy Progress, LLC, the Companies, the
13 Companies' advisors, and the independent banks that
14 will likely underwrite the storm recovery bond issue.

15 A key concept for the Commission to consider
16 is whether or not the parties involved have what is
17 often referred to as a fiduciary relationship, as
18 opposed to underwriters, advisors, companies acting
19 primarily in their own financial interest. In broad
20 terms, a service provider that has a fiduciary
21 responsibility to its client commits to act in the
22 client's best interests to the exclusion of any
23 contrary interests. Where a fiduciary relationship
24 exists, the client should be comfortable that the

1 service provider is looking out for the client's best
2 interests. The issue of whether a fiduciary
3 relationship exists impacts what the Commission should
4 consider in deciding how to evaluate information it
5 receives from different parties in the proposed
6 transaction. In my experience, for example,
7 underwriters claim that they have no fiduciary
8 relationship to issuers. Underwriting agreements
9 prepared by counsel for the underwriters now typically
10 include a specific declaration that underwriters have
11 no fiduciary relationship with the issuer. Issuers are
12 frequently asked to acknowledge this affirmatively in
13 the underwriting agreement.

14 Bond underwriters will typically propose an
15 offering process, including bond pricing, whereby the
16 underwriters use their, quote, professional judgment,
17 unquote, in establishing price guidance and change that
18 price guidance, quote, solely in their professional
19 judgment, unquote. This is what the Companies' witness
20 Atkins has testified. However, the underwriters act in
21 their own benefit and cannot always be counted on to
22 act solely in behalf of the issuer. Pricing is
23 arguably the most important component of offering
24 securities in the market. I believe this is a

1 compelling reason why bond issuers need to be very
2 active in the offering process to protect their own
3 interests.

4 In response to data request questions
5 inquiring if underwriters of securities have a duty to
6 the issuer, and if those -- of those securities, and if
7 it is a fiduciary duty, the Companies' witness Heath
8 stated that the underwriters do not have a fiduciary
9 duty to the issuer. In responding to PS DR 2-2(g),
10 witness Heath acknowledged that the engagement letters
11 between the Companies, Guggenheim Securities, and
12 Atkins Capital do not create a fiduciary relationship
13 between the parties.

14 In contrast, as financial advisor to the
15 Public Staff, Saber Partners considers itself as having
16 a fiduciary duty to the North Carolina ratepayers.

17 The storm recovery bond transaction is
18 different from normal corporate debt issues in which
19 the issuer has a direct interest in minimizing the cost
20 of the transaction in order to maximize economics for
21 its shareholders.

22 For traditional utility debt issues, as well,
23 incentives exist to minimize the costs of the
24 transaction. Here the Companies propose that the storm

1 recovery bonds will be issued by special purpose
2 entities, SPEs. This is simply a mechanism to
3 facilitate the transfer of funds from the ratepayers to
4 the Companies, while the ratepayers alone will
5 ultimately bear all transaction costs and all costs of
6 repaying the storm recovery bonds. The Companies will
7 receive the net proceeds of the bonds to recover
8 previously incurred costs.

9 While I do not doubt that the Companies would
10 desire that the ratepayers incur low storm recovery
11 charges, the Companies' main motivation is to receive
12 the debt proceeds in a timely, efficient manner.
13 Therefore, the Companies do not share the same
14 incentives to achieve the lowest overall cost of funds.
15 It is left to the Commission and the Public Staff to
16 ensure that the ratepayers achieve the lowest overall
17 cost of funds and the bonds and the lowest storm
18 recovery charges consistent with market conditions at
19 the time the bonds are priced. I believe that they
20 need to be fully involved in working in a cooperative
21 way with the Companies and the Companies' financial
22 advisor to achieve that objective. That will require
23 optimal structuring and marketing of the storm recovery
24 bond issue.

1 I believe that the bond team for the storm
2 recovery bond issue should consist of Companies; the
3 Companies' advisor, provided such advisor is not one of
4 the banks acting as underwriter for the transaction;
5 the Commission, either directly or through a designated
6 staff member; the Public Staff; and the independent
7 advisors and counsel. I believe it is very important
8 for the lead Commission representative to be closely
9 involved in the project. There are many complexities,
10 and this is probably not the type of work that
11 Commissioners undertake on a regular basis. It is
12 important that the bond team operate independently and
13 entirely in the interest of the ratepayers and not
14 include any of the underwriting banks due to their
15 inherent conflict of interest discussed above. All
16 members of the bond team should have a fiduciary
17 relationship with either the Companies, the Commission,
18 or the Public Staff.

19 Decisions of the Bond Team should be a shared
20 responsibility of its members, with the Commission's
21 representative in a position to make the final decision
22 on a timely basis, often in real time during the final
23 pricing process, in the event of any disagreements
24 among Bond Team members.

1 In my many years overseeing ExxonMobil's
2 capital markets activities, I learned that bond issues
3 could almost always be done at lower rates than the
4 best market preliminary indications given by the banks.
5 This was true despite the fact that ExxonMobil was a
6 well-known and coveted AAA-rated debt issuer. Active
7 involvement by ExxonMobil to create competition among
8 the banks and to demand the best execution consistently
9 added value.

10 It is also true that all AAA and AAA(sf),
11 meaning structured finance, rated debt is not viewed
12 alike by investors in the debt capital markets. For
13 example, when I worked at ExxonMobil, AAA-rated
14 ExxonMobil or federal agency credits would command
15 better pricing than most AAA-rated structured debt
16 securities which were backed solely by a pool of
17 intangible contract rights, such as mortgages or credit
18 card receivables.

19 In summary, the proposed storm recovery bonds
20 should achieve a AAA(sf) rating and perform well in the
21 market. But superior performance is not automatic
22 since all AAA and AAA(sf)-rated bonds do not trade
23 alike. The key takeaway should be that, while factors
24 such as underwriters' professional opinions are

1 valuable, underwriters do not have any fiduciary
2 responsibility to the ratepayer. Similarly, the
3 Companies' primary responsibility is to their own
4 shareholders. Therefore, the Commission, the Public
5 Staff, and their independent financial advisors are in
6 the primary position of having to look out for the
7 ratepayers' best interests. It is critical that they
8 play an active role in all aspects of the transaction.
9 They must be willing to invest all the time necessary
10 in the structuring and take an aggressive stance during
11 the marketing process to capture the lowest cost of
12 financing and the lowest storm recovery charges for the
13 ratepayers. This should involve full participation in
14 the transaction with the Companies and the bond
15 underwriters, and, if required, timely decision-making
16 by the Commission to resolve any potential financing
17 issues in the ratepayers' best interests.

18 This completes my summary. Thank you.

19 MR. GRANTMYRE: Thank you. The witness
20 would be available for cross examination after the
21 other two panelists have presented their testimony.
22 Thank you.

23 MR. CREECH: Next, Chair Mitchell, we'd
24 like to call Hyman Schoenblum.

1 THE WITNESS: (Hyman Schoenblum) Good
2 morning.

3 DIRECT EXAMINATION BY MR. CREECH:

4 Q. Good morning. Good morning. Mr. Schoenblum,
5 can you turn up your volume there just a moment. I'll
6 try to do it the same on mine perhaps. Maybe it's me.
7 There we go.

8 Mr. Schoenblum, please state your name and
9 business address for the record.

10 A. (Hyman Schoenblum) How's that?

11 Q. Perfect. Please state your name and business
12 address for the record.

13 A. My name is Hyman Schoenblum. My business
14 address is 260 Madison Avenue, New York, New York
15 10016.

16 Q. And today you're testify on behalf of the
17 Public Staff; is that correct?

18 A. That's correct.

19 Q. Mr. Schoenblum, did you cause to be filed in
20 this docket --

21 A. I'm not hearing you.

22 Q. Can you hear me now?

23 A. Yes.

24 Q. Did you cause to be filed in this docket, on

1 December 21, 2020, direct testimony consisting of
2 56 pages and 2 exhibits?

3 A. Yes.

4 Q. Do you have any corrections to your
5 testimony?

6 A. No.

7 Q. If you were asked the same questions today,
8 would your answers be the same?

9 A. Yes.

10 MR. CREECH: Chair Mitchell, at this
11 time I move that Mr. Schoenblum's prefilled direct
12 testimony be copied into the record as if given
13 orally from the stand and that his two exhibits be
14 marked for identification as premarked in the
15 filing.

16 CHAIR MITCHELL: All right. Hearing no
17 objection, Mr. Creech, to your motion, it is
18 allowed.

19 MR. CREECH: Thank you.

20 (Schoenblum Exhibits 1 and 2, were
21 identified as they were marked when
22 prefilled.)

23 (Whereupon, the prefilled direct
24 testimony of Hyman Schoenblum was copied

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into the record as if given orally from
the stand.)

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

Docket No. E-2, Sub 1262

Docket No. E-7, Sub 1243

In the Matter of		
Joint Petition of Duke Energy	)	DIRECT TESTIMONY OF
Carolinas, LLC and Duke Energy	)	HYMAN SCHOENBLUM,
Progress, LLC Issuance of Storm	)	SENIOR ADVISOR – SABER
Recovery Financing Orders	)	PARTNERS, LLC

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

**Docket No. E-2, Sub 1262
Docket No. E-7, Sub 1243**

Direct Testimony of

Hyman Schoenblum, Senior Advisor

Saber Partners, LLC

December 21, 2020

TESTIMONY OF HYMAN SCHOENBLUM
DECEMBER 21, 2020

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INTRODUCTION

1 **Q. PLEASE STATE YOUR NAME AND ADDRESS.**

2 A. Hyman Schoenblum, 260 Madison Avenue, Suite 8019, New York,
3 NY 10016.

4 **Q. WHAT IS YOUR POSITION WITH SABER PARTNERS LLC?**

5 A. I am a Senior Advisor to Saber Partners, LLC (Saber Partners or
6 Saber).

7 **Q. ARE YOU SPONSORING ANY EXHIBITS?**

8 A. Yes. I am sponsoring the following exhibits:

9 Schoenblum Exhibit 1, Barclays Technical Note: Classification of
10 Duke Energy Florida Project Finance, LLC Bonds

11 Schoenblum Exhibit 2, Asset Securitization Report, Duke Utility Fee
12 Securitization Sets Important Precedent, June 21, 2016

13 In addition, except as otherwise defined in this testimony, terms have
14 the meanings assigned to them in the Glossary attached as the final
15 exhibit to the testimonies of Public Staff witnesses Joseph Fichera
16 and Paul Sutherland.

17 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND**
18 **PROFESSIONAL EXPERIENCE.**

1 A. I have an undergraduate BBA degree in Accounting from Baruch
2 College in New York City and a Master's Degree in Finance from the
3 same school.

4 I worked for 35 years at the Consolidated Edison Company of New
5 York, Inc. (Con Ed), in various financial management capacities. Con
6 Ed is the largest electric utility in the State of New York.

7 At various times, I served as Con Ed's Vice President and Treasurer;
8 Vice President and Controller; Vice President of Strategic Planning;
9 and Chief Financial Officer of Con Ed's wholly owned subsidiary,
10 Orange and Rockland Utilities. I also led a task force to prepare Con
11 Ed for the financial impacts of competition in New York State. While
12 in those positions, I also served as a key spokesperson in Con Ed's
13 investor relations effort, meeting regularly with institutional investors,
14 investment banking research professionals and others.

15 For many years, I was a senior financial officer at Con Ed, with
16 expertise in financial matters as well as ratemaking policies and
17 practices of regulated utilities. I participated in the review of financial
18 transactions (debt and equity offerings, mergers and acquisitions);
19 the analyses of ratemaking policies and proposals; the evaluation of
20 the timing and method of financing decisions; the litigation of rate
21 cases; and the assessment of capital investment determinations.

1 Decision making at Con Ed in these matters rested with the parent
2 company's Chief Financial Officer (CFO) and Chief Executive Officer
3 (CEO).

4 After retiring from Con Ed, I joined the Maimonides Medical Center
5 of Brooklyn, New York, as their Vice President of Internal Audit. I
6 retired from Maimonides in 2018.

7 **Q. WHAT SPECIFIC ACTIVITIES DID YOU UNDERTAKE IN THESE**
8 **ROLES?**

9 A. As Vice President of Strategic Planning at Con Ed, I was the senior
10 financial executive on the Strategic Planning Team responsible for
11 identifying and investigating the potential value to shareholders and
12 ratepayers of mergers and acquisitions for Con Ed. I worked with
13 numerous investment bankers to identify merger candidates for the
14 company. This required detailed and intensive review of operating
15 and financial information of potential acquirees and reporting the
16 results to senior management.

17 I played a key financial role in Con Ed's completed merger with
18 Orange and Rockland Utilities. I was also instrumental in Con Ed's
19 announced, but not completed, merger with Northeast Utilities, as
20 well as other potential Con Ed mergers which were identified and
21 evaluated, but not pursued. I also testified before the New York State
22 (NYS) Public Service Commission and before the New Hampshire

1 Public Service Commission regarding the ratepayer impacts in the
2 uncompleted merger with Northeast Utilities.

3 This merger activity required careful review of operating and financial
4 risks and evaluation of the fairness opinions that the investment
5 bankers offered in support of the proposed merger. The proposed
6 acquisition of Northeast Utilities was rejected when we identified
7 risks that put the fairness opinions in jeopardy.

8 I also participated in the process of identifying and evaluating other
9 investment opportunities for Con Ed to expand into unregulated and
10 competitive businesses, such as power generation and
11 telecommunications. In this capacity, I worked closely with a variety
12 of participants in the financial community including investment
13 bankers, financial advisors, and institutional investors.

14 A key element to this activity was the evaluation of the
15 representations of the bankers and consultants seeking to convince
16 the company of the efficacy of the investments.

17 As deregulation in New York State began to unfold, I was appointed
18 to head the financial team that would evaluate its impact on the
19 company's long-term financial forecasts and to assist in the
20 divestiture of generation assets so as to implement the deregulated
21 energy markets.

1 As Con Ed's Vice President and Controller, I played a central role in
2 the coordination of Con Ed's electric, gas, and steam rate cases,
3 testifying numerous times before the NYS Public Service
4 Commission on a variety of financial and operating matters. I testified
5 regarding cost of capital issues as well as on a wide range of
6 operating revenues and expenses. I assisted our rate attorneys in
7 negotiating appropriate rate settlement agreements.

8 As Vice President and Controller, I was responsible for the
9 preparation of the periodic financial results of Con Ed and its
10 subsidiaries, the filing of Securities & Exchange Commission annual
11 and quarterly reports, and reporting to the Board of Directors on a
12 monthly basis on financial results. I was also in charge of the
13 company's operating and capital budgets and the development of
14 long-term financial forecasts.

15 A key element to this activity was working with the outside auditors
16 to ensure that the "opinions" they rendered would fairly represent the
17 results and risks inherent in the financial statements.

18 Of equal importance, was the passage of the Sarbanes-Oxley Act of
19 2002 (SOX) which mandated that senior corporate officers certify in
20 writing that the company's financial statements "comply with SEC
21 disclosure requirements and fairly present in all material aspects the
22 operations and financial condition of the issuer" (Section 302 of
23 SOX), Officers who sign off on financial statements that they know

1 to be inaccurate are subject to criminal penalties, including prison
2 terms. This added a heightened level of review and scrutiny to
3 ensure that the “opinions” set forth by management were fair,
4 reasonable and accurate.

5 As Con Ed’s Vice President and Treasurer, I participated with the
6 Finance team in coordinating Con Ed’s capital financings
7 (approximately \$1 billion over a number of traditional debt
8 transactions) and cash management needs. This required intensive
9 interaction with the company’s bankers, its senior management, and
10 the Finance Committee of the Board of Trustees in various aspects
11 of pricing and selling the debt issuances. I also interacted with the
12 rating agencies, as appropriate.

13 As Treasurer, I was also one of the named fiduciaries of Con Ed’s
14 Pension Plan responsible for administration of the plan, hiring of fund
15 managers, and setting the appropriate investment allocations for the
16 plan.

17 Lastly, I helped supervise Con Ed’s vast real estate portfolio and
18 began the process of divesting significant unneeded parcels of
19 property in midtown Manhattan. This later resulted in significant
20 gains to Con Ed, its ratepayers, and its shareholders.

21 **Q. WHILE AT CON ED, DID YOU HAVE ANY EXPERIENCE WITH**
22 **UTILITY SECURITIZATION/RATEPAYER-BACKED BONDS?**

1 A. As Treasurer, I assisted in a corporate review of a potential
2 Ratepayer-Backed Bond transaction for Con Ed. Our team analyzed
3 this financing mechanism, the market and potential to benefit Con Ed
4 and its ratepayers. New York State did not have enabling legislation
5 that was necessary for a AAA rating. Although there was a proposal
6 to undertake it under the commission's existing authority, it was
7 never tested.

8 **Q. DID YOU HAVE DIRECT EXPERIENCE WITH INSTITUTIONAL**
9 **AND OTHER INVESTORS, EITHER AS RELATING TO CON ED IN**
10 **PARTICULAR OR WITH REGARDS TO THE UTILITY INDUSTRY**
11 **IN GENERAL?**

12 A. While serving in the above-mentioned positions, I played a visible
13 leadership role in Con Ed's relationship with the Wall Street
14 community. Along with others, I met very frequently with institutional
15 investors, fund managers, stock and bond research analysts and the
16 media to present Con Ed's financial position to the investment
17 community. When adverse financial events took place, or when rate
18 cases were being litigated and decided, I was often on the phone
19 with investors and the financial press for many hours describing the
20 potential implications. These activities enabled me to develop a solid
21 relationship with the investment community, and they viewed me as
22 a highly trustworthy individual, which inured to the benefit of the
23 company.

1 In addition, during my employment at Con Ed, I served on many
2 committees and task forces of the Edison Electric Institute (EEI), the
3 electric industry's primary trade organization. I served as chairman
4 of EEI's Accounting Principles Committee in the early 1980s.

5 I also attended many industry-wide financial conferences and
6 discussed financial practices and policies with my peers. I was often
7 invited to participate in panels alongside utility CFOs and CEOs to
8 discuss financial issues affecting the utility industry, particularly in
9 relation to the impacts of deregulation.

10 **Q. IN WHAT OTHER FINANCIAL RELATED ACTIVITIES WERE YOU**
11 **INVOLVED?**

12 A. From 2000 to 2006, I served as a member of the Board of Trustees
13 of Maimonides Medical Center in Brooklyn and was on their Audit,
14 Finance, Pensions, Investments and Medical Matters Committees.
15 In 2006, I retired from Con Ed and became the Vice President of
16 Internal Audit at Maimonides Medical Center. In that role, I was
17 responsible for financial and operating audits and for investigating
18 fraud. I reported quarterly to the Audit Committee of the Board and
19 attended Board and committee meetings. I retired from the medical
20 center in 2018.

21 **Q. HAVE YOU HAD RECENT EXPERIENCE WITH RATEPAYER-**
22 **BACKED BONDS?**

1 A. Yes. In 2015, I provided direct testimony to the Florida Public Service
2 Commission (FPSC) on the Duke Energy Florida (DEF) \$1.3 billion
3 Ratepayer-Backed Bond transaction which refinanced the
4 unrecovered cost of a retired nuclear power plant. I testified on a
5 number of issues including the need for close Commission oversight
6 after the issuance of a Financing Order and the benefits of a “Bond
7 Team,” which included an outside financial advisor to the
8 Commission and its staff.

9 I also participated in many aspects of the negotiations between the
10 parties, including the FPSC staff, as well as the interactions between
11 the Bond Team and the investment bankers hired to manage the
12 issuance of the proposed securitized nuclear asset-recovery bonds.

13 I also had a similar role in an earlier issuance of Ratepayer-Backed
14 Bonds in Florida for the recovery of storm costs by Florida Power and
15 Light Company (FPL).

16 **Q. HAVE YOU TESTIFIED IN OTHER STATES ON THIS SUBJECT**
17 **MATTER?**

18 A. Yes. In 2018, I submitted testimony representing Saber Partners that
19 had been hired by the California Community Choice Association to
20 evaluate the risks and benefits of Ratepayer-Backed Bonds to the
21 consumers and shareholders of the California utilities.

1 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

2 A. The primary purpose of my testimony is to explain why there is a
3 need for active Commission involvement through its experts and
4 independent advisors in the structuring, marketing and pricing of the
5 proposed storm recovery Ratepayer-Backed Bond offering. I will
6 distinguish between the regulatory oversight applied to Ratepayer-
7 Backed Bonds and the oversight applicable to traditional utility debt
8 offerings and why intense oversight of Ratepayer-Backed Bond
9 transactions is necessary. I will show how the two types of bonds do
10 not provide the same incentives to achieve the lowest costs to the
11 customer and will also discuss briefly why the “lowest storm recovery
12 charge” standard and maximum present value savings for
13 ratepayers, based on information available through the date of
14 pricing, are appropriate for this transaction. Lastly, I will address the
15 importance of independent fiduciary opinions to ensure that
16 ratepayers are receiving the maximum benefits of the Ratepayer-
17 Backed Bond transaction, without being subjected to potential
18 conflicts of interest.

19 **CONDITIONS FOR A SUCCESSFUL INITIAL PUBLIC OFFERING**
20 **OF RATEPAYER-BACKED BONDS**

21 **Q. WHAT MAKES A SUCCESSFUL INITIAL PUBLIC OFFERING OF**
22 **RATEPAYER-BACKED BONDS FOR RATEPAYERS AND THE**
23 **UTILITY?**

1 A. First, as Witnesses Abramson and Klein point out, the North Carolina
2 Utilities Commission (Commission) is establishing a Ratepayer-
3 Backed Bond program for North Carolina’s investor-owned utilities
4 and not just doing a one-off transaction. It is important that the first
5 transaction under a new program firmly establish the policies and
6 principles that future transactions will follow.

7 A successful Ratepayer-Backed Bond offering produces the greatest
8 economic value from the newly created property that was authorized
9 by the authorizing legislation, by raising funds at the lowest possible
10 cost and least exposure to liability for ratepayers. If the measure of
11 success were to simply sell the security created by Securitization and
12 raise cash, regardless of the cost of the security, a “successful”
13 Ratepayer-Backed Bond transaction would need very little attention
14 because there are many investors that want a high-quality, high-
15 yielding investment product. But, that would not be a successful
16 transaction for the ratepayers responsible for paying the charges.
17 Nor would it benefit the Commission that has given up future
18 regulatory review of the costs and is unequivocally committed to
19 adjusting future securitization charges, as needed.

20 **Q. IN 2015, DEF FILED A PETITION AND RELATED TESTIMONY**
21 **FOR THE SECURITIZATION OF \$1.3 BILLION TO RECOVER THE**
22 **COSTS OF A RETIRED NUCLEAR PLANT. IN THAT**
23 **PROCEEDING, THE PARTIES, INCLUDING DEF, REACHED A**

1 **STIPULATION FOR THE CREATION OF A “BOND TEAM,”**
2 **INCLUDING AN INDEPENDENT FINANCIAL ADVISOR, TO**
3 **WORK COLLABORATIVELY WITH THE COMMISSION STAFF**
4 **AND DEF TOWARDS A SUCCESSFUL BOND ISSUANCE.**
5 **NEITHER WITNESS ATKINS NOR WITNESS HEATH MAKE A**
6 **“BOND TEAM” PROPOSAL FOR THE NORTH CAROLINA**
7 **UTILITIES COMMISSION AND PUBLIC STAFF’S**
8 **PARTICIPATION IN THE COMPANIES SECURITIZATION. WHAT**
9 **IS YOUR REACTION?**

10 A. To put it simply, I would not tamper with success. The Bond Team
11 approach resulted in a highly praised bond offering for DEF, which
12 yielded significant savings to ratepayers. In the DEF Ratepayer-
13 Backed Bond transaction, I was able to observe first-hand the
14 benefits of this collaborative process and its impact on the final
15 results on a successful offering. True, there were instances, as in
16 any negotiation, where the parties did not fully agree on the process,
17 but by working collaboratively, the Bond Team was able to reach a
18 necessary consensus.

19 I believe that the Commission, Public Staff, their independent
20 advisors and the Companies need to be integral and equal partners
21 in all aspects of the process. All of these parties need to play an
22 active and visible role in presenting the proposed storm recovery
23 bonds to the capital markets.

1 In my view, the process needs to be viewed by investors and all
2 participants as a joint, collaborative process, so that investors and
3 ratepayers are assured that they are well protected.

4 Any traditional utility financing will have meaningful regulatory
5 oversight, and the ratemaking process generally provides that
6 oversight on an ongoing basis. In the case of this storm recovery
7 Ratepayer-Backed Bond financing, however, the constraints
8 imposed by the enabling statute appear to prohibit “after-the-fact”
9 reviews for prudence in evaluating any aspect of the structuring,
10 marketing and pricing of these bonds. In addition, the State also
11 pledges not to take any action that puts the repayment of the storm
12 recovery bonds, and related interest, at risk.

13 In light of these after-the-fact ongoing constraints, Commission
14 oversight at the outset needs to be expanded to include Commission
15 and Public Staff involvement critical to the maintenance of the credit
16 value. There needs to be an understanding by investors that the
17 regulator and ratepayers fully support all aspects of the offering and
18 that there is likely little, if any, “political” risk to the storm recovery
19 bond. For example, if the record clearly shows that the Commission
20 and Public Staff fully supported and approved all aspects of the
21 offering, it becomes less likely that future elected officials or
22 appointees at the Commission or Public Staff will attempt to
23 challenge the bond structure or the storm recovery charge.

1 In light of their responsibilities relating to storm recovery bonds, the
2 Commission and Public Staff need to be more involved in the
3 structuring, marketing, and pricing process so as to be thoroughly
4 informed, able to assimilate the impact of structuring changes, and
5 to understand the decisive elements included in determining the
6 pricing guidance. To be effective in meeting its mandate in this
7 financing, the Commission needs greater information and
8 involvement, not less. Existing legislation directs Public Staff to be
9 an integral voice in matters affecting ratepayers and to provide the
10 Commission with the necessary information and expertise to make
11 informed decisions.

12 It is my opinion that the Financing Order should provide for the
13 creation of a Bond Team which will ensure that the Commission, as
14 well as Public Staff and their respective financial advisors, will be
15 directly and visibly involved throughout the structuring, marketing,
16 and pricing process.

17 **MAXIMIZING RATEPAYER BENEFITS**

18 **Q. HOW CAN THE BENEFITS TO RATEPAYERS BE MAXIMIZED?**

19 A. One of the hallmarks of Ratepayer-Backed Bond transactions is that
20 the financing orders are irrevocable: the state agrees never to impair
21 the right of the bondholders to the special charge as it is adjusted
22 periodically to repay the bonds in full. This is a key feature in helping

1 to secure a AAA rating. But an irrevocable Financing Order also
2 forfeits the Commission's traditional retrospective review function
3 after the bonds are issued. This is why it is essential for the
4 Commission, Public Staff, and the Companies to create a
5 collaborative, cooperative process. The best way to protect
6 ratepayers is to provide for a clear standard to evaluate proposals
7 and for Commission approval of all future decisions affecting
8 ratepayers before they are made final when the bonds are issued.
9 The Commission should not make final decisions based on draft
10 language submitted as exhibits to the Joint Petition or exhibits to
11 testimony, but on final terms and conditions. For this to be a
12 meaningful review and decision process, it cannot be restricted or
13 restrained in terms of time and consideration. By adopting the "best
14 practices" procedures summarized in this testimony, the
15 Commission will be "at the table" for all negotiations affecting
16 ratepayers in advance of any decisions affecting such ratepayers.
17 The Commission and the Companies should work in a collaborative
18 process when negotiating with each other and with underwriters and
19 investors.

20 **Q. DOES RATEMAKING FOR RATEPAYER-BACKED BONDS**
21 **FUNDAMENTALLY DIFFER FROM STANDARD UTILITY**
22 **RATEMAKING?**

1 A. Yes, it does. Standard utility ratemaking generally provides
2 appropriate incentives for utility debt issuers to achieve both the
3 lowest overall cost to customers and favorable returns for
4 shareholders. The Commission has the authority to review all actions
5 by utilities, including its bond issuances, and to disallow imprudent
6 expenditures when setting appropriate rates at any time.

7 Further, issuers of standard utility securities are incentivized to
8 reduce interest rates on their debt offerings and other ongoing
9 financing costs below the target level set in rates through the
10 standard ratemaking process. By doing so, the utility can either
11 increase its rate of return or offset other unavoidable cost increases
12 not yet included in rates. This is particularly important if the utility is
13 operating under a long-term rate settlement agreement. In the
14 context of the issuance of traditional utility debt securities, these are
15 powerful tools in the Commission's hands to achieve a lowest overall
16 cost result and discharge the Commission's responsibilities to
17 ratepayers.

18 When I served as Treasurer at one of the largest utilities in the
19 country, and we were in the process of issuing debt, I was always
20 cognizant that we might easily be second-guessed by the NYS Public
21 Service Commission questioning the results of the transaction in a
22 future rate proceeding. That provided an appropriate incentive to
23 structure and price the transaction very carefully.

1 However, this very strong incentive is not present with regard to
2 Ratepayer-Backed Bonds. As described above, the Commission's
3 hands are severely constrained. Unlimited post-issuance reviews are
4 prohibited because such reviews would threaten the viability of the
5 AAA rating. Thus, appropriate safeguards need to be implemented
6 at the outset of the process.

7 Furthermore, while the Companies have a general business interest
8 to keep overall customer rates low, the utilities will have no obligation
9 to repay the storm-recovery bonds and will have no responsibility to
10 pay any of the costs.

11 The Companies will have a small capital investment in the AAA
12 finance subsidiary which they are guaranteed to receive back at the
13 end of the transaction through storm recovery charges. All other
14 costs will be borne directly by the ratepayers, and the traditional
15 regulatory checks and balances will be missing.

16 In fact, the highest priority of the Companies in this transaction will
17 be to get the issuance done quickly, with cost taking a lower priority.

18 Getting the issuance done quickly will be the highest priority of the
19 Underwriters as well.

20 **Q. IS THERE ANOTHER MAJOR REASON WHY COMMISSION AND**
21 **PUBLIC STAFF INVOLVEMENT IS NECESSARY?**

1 A. Yes. Generally, the interests of Underwriters are fundamentally
2 adverse to the interests of ratepayers. Underwriters will want to
3 negotiate for relatively high rates of interest so that the bonds can be
4 sold with the least effort, satisfying the desires of their investors for
5 high interest rates relative to competing investments. Underwriters
6 will also negotiate aggressively for the highest possible underwriting
7 fees. There is nothing inherently wrong about this process. It is part
8 of a “market system” where each participant acts in his or her own
9 economic interest. But, because 100 percent of the economic burden
10 will be borne by the ratepayers, it is wise to keep this in mind when
11 negotiating Underwriter fees, the marketing plan, and final prices
12 with Underwriters and investors. Deferring to the Underwriters’
13 “professional judgement,” as Witnesses Atkins and Heath suggest,
14 is not always in the best interest of ratepayers who are paying all of
15 the bills.

16 **Q. ARE THESE THE PRIMARY REASONS FOR THE COMMISSION**
17 **AND PUBLIC STAFF TO BE INVOLVED IN ALL STEPS OF THE**
18 **SECURITIZATION PROCESS BEFORE THE STORM RECOVERY**
19 **BONDS ARE ISSUED?**

20 A. Yes. The only prudent and reasonable approach, with ample
21 precedent in other Ratepayer-Backed Bond transactions, is direct
22 Commission and Public Staff involvement in all the steps of the
23 process. That will provide the Commission with the essential

1 information to approve this storm recovery bond issuance as
2 unequivocally protecting ratepayers' interests and help achieve the
3 lowest storm recovery charges.

4 The Commission should be actively engaged in receiving from Public
5 Staff and the Companies market pricing information, and in creating
6 an investor marketing strategy and outreach to assure the
7 Commission's thorough understanding and effective decision
8 making in a timely fashion. An inefficient transaction and needlessly
9 higher storm recovery charges could result from a lack of
10 Commission oversight. Active participation with the Public Staff and
11 its advisors is the way to ensure proper ratepayer protection.

12 **Q. IS IT IMPORTANT TO HAVE RATEPAYER PROTECTIONS IN**
13 **THE FINANCING ORDER AND THE BOND TRANSACTION**
14 **DOCUMENTS AS WELL?**

15 A. Yes. In a complex legal arrangement such as a Ratepayer-Backed
16 Bond transaction, terms, conditions, representations and warranties
17 concerning all contracts need to be evaluated from an arm's length,
18 dispassionate perspective. The risks, costs, and liabilities should be
19 independently evaluated, and policies independently developed.

20 From the Commission's and ratepayers' perspective, the storm
21 recovery bonds will be issued under an irrevocable Financing Order
22 that cannot be changed by the Commission after the bonds have
23 been issued. The term of the bonds could be 15-20 years or longer.

1 In addition, the Companies and their respective Special Purpose
2 Entity (SPE) issuers will enter into servicing agreements under which
3 the sponsoring utility will bill, collect and remit the storm recovery
4 charge to a bond trustee for the account of the SPE issuer. Like any
5 other contract for services, that servicing agreement will have
6 provisions concerning performance, care, liabilities, and indemnities.
7 All these could affect ratepayers at any time during the life of the
8 storm recovery bonds. Yet, the servicing agreements are essentially
9 between affiliated parties with all the liabilities associated with the
10 agreements falling to ratepayers under the storm recovery charge
11 and the true-up mechanism.

12 Saber Partners strongly believes regulatory oversight should be
13 preserved concerning the servicing agreements and other
14 transaction documents for the life of the storm recovery bonds. With
15 an increasing number of mergers in the electric industry, it is
16 important for the Commission to look beyond the next few years and
17 put in place ratepayer protections that survive even in the case of a
18 merger and new management. Ever-changing corporate structures
19 need scrutiny by the Commission since future owners may have a
20 different attitude about this transaction 10-15 years or longer into the
21 future.

22 **Q. IN YOUR VIEW, SHOULD THE COMMISSION GIVE THE**
23 **COMPANIES BROAD FLEXIBILITY TO ESTABLISH THE FINAL**

1 **TERMS AND CONDITIONS OF THE BONDS AS SUGGESTED BY**
2 **WITNESSES ATKINS AND HEATH?**

3 A. No. Were these normal utility bonds subject to standard review and
4 approval in the ratemaking process, the Commission could easily
5 grant that broad flexibility because the Commission would have the
6 authority for an unlimited after-the-fact review. In this case, however,
7 the Commission does not have that opportunity, as described earlier.
8 As such, the Ordering Paragraphs need to recognize that the final
9 terms and conditions will be determined in a joint, collaborative
10 process with the Commission, Public Staff and/or its independent
11 advisors participating actively, visibly, and in real-time.

12 **Q. SHOULD AT LEAST SOME BOND TEAM PARTICIPANTS HAVE**
13 **A FIDUCIARY RELATIONSHIP WITH THE UTILITIES, THE**
14 **COMMISSION OR PUBLIC STAFF, AND IF SO, WHY?**

15 A. Yes. As described in the testimony of Witness Maher, it is important
16 that the Companies and the Commission receive conflict-free advice
17 from experts when making their decisions. In this regard, such
18 experts should have a fiduciary relationship with either the utilities,
19 the Commission or Public Staff. Thus, the Underwriters of this storm
20 recovery bond transaction should not be conflicted by, for example,
21 providing consulting advice to the utilities on the same transaction.

22 **Q. DO YOU KNOW IF THE UTILITIES PLAN TO USE**
23 **UNDERWRITERS WHO WILL ALSO PROVIDE CONSULTING**

1 **ADVICE TO THEM ON THE SAME RATEPAYER-BACKED**
2 **BONDS IN THIS CASE, AND IF SO, WHY WOULD THIS POSE A**
3 **CONFLICT?**

4 A. I do not know definitively. However, Witnesses Atkins and Heath,
5 who are testifying on behalf of the Companies, have proposed that
6 these securitized storm recovery bonds be sold in a negotiated sale
7 through a group of pre-selected Underwriters. In response to PS DR
8 2-2(h), Witness Heath states: “For the vast majority of utility
9 securitizations not issued by municipal entities, with only a very few
10 exceptions, it is the market practice for the structuring advisor to also
11 serve as a lead underwriter.” For the reasons outlined in my
12 testimony above, a conflict of interest arises whenever the same firm
13 provides consulting advice to an issuer and then serves as the lead
14 Underwriter for the issuer on the same transaction.

15 In addition, many of the largest Underwriters in the country have also
16 been utilized as both an Underwriter and a Bookrunning Manager in
17 other Ratepayer-Backed Bond issuances. As such, there is a strong
18 possibility that one of the pre-selected Underwriters may also
19 become a Bookrunning Manager.

20 In fact, given Witness Atkins’ strong historical ties with Morgan
21 Stanley, I would not be surprised if Morgan Stanley were conflicted
22 in this manner. In my view, this represents a conflict of interest and
23 should be avoided, if possible.

1 In a typical corporate bond issuance, the issuer often states in the
2 prospectus, under the heading "Underwriters (Conflict of Interest)",
3 that some of the Underwriters of the issuance also provide financial
4 advisory services for which they receive payment rather than simply
5 disclosing a conflict of interest.

6 In fact, as mentioned above, Witness Heath in response to Data
7 Request PS-DR 2-2(h) states that, from his perspective, the
8 structuring advisors "due to their familiarity with, and their experience
9 participating in the regulatory testimony and interrogatory process,
10 are often in the best position to serve as lead underwriter of
11 Securitization bonds". It is obviously convenient to have the advisor
12 also act as Underwriter, but I question the appropriateness of this
13 arrangement. From my perspective, we need to question whether the
14 lead Underwriters will have the proper and necessary incentives in
15 this transaction.

16 I understand that under North Carolina storm recovery bond statute,
17 the Commission will not have the ability to assess this Ratepayer-
18 Backed Bond transaction on a post-issuance basis. Thus, pre-
19 issuance guidelines are definitely advisable.

20 **RATEPAYER-BACKED BOND OFFERING PRECEDENTS**
21 **RELEVANT TO NORTH CAROLINA AND THE JOINT PETITION**

22 **Q. REGARDING RATEPAYER-BACKED BONDS ISSUED IN OTHER**
23 **STATES, HAVE COMMISSIONS BEEN ACTIVELY INVOLVED IN**

1 **THE STRUCTURING, MARKETING, AND PRICING OF THESE**
2 **TRANSACTIONS?**

3 A. Yes. Commissions in Florida, Texas, New Jersey, West Virginia,
4 Ohio, and Louisiana have been actively involved in the structuring,
5 marketing and pricing of Ratepayer-Backed Bonds. The degree of
6 involvement and success has varied, but involvement in a post-
7 financing order/pre-bond issuance review process is consistent.

8 The Texas Commission has had one of the most active post-
9 financing order participation regimes, particularly in the first six
10 Ratepayer-Backed Bond offerings that it approved. Witness
11 Rebecca Klein, former Chair of the Public Utility Commission of
12 Texas (PUCT), testifies at length about her positive experiences
13 regarding the involvement of the PUCT and its financial advisor in
14 the Securitization process.

15 Florida and West Virginia have also been very successful in
16 protecting ratepayers' interests through their financing orders that
17 were based on "best practices."

18 With regards to North Carolina, since this will be the first Ratepayer-
19 Backed Bond transaction under the State's storm recovery bond
20 statute, it is certainly advisable, even critical, that the Commission
21 and the Public Staff have active involvement in all aspects of the
22 transaction.

1 **Q. CAN YOU DESCRIBE THE RESULTS THAT WERE ACHIEVED**
2 **BY THE ACTIVE INVOLVEMENT OF COMMISSIONS IN THE**
3 **STRUCTURING, MARKETING, AND PRICING OF RATEPAYER-**
4 **BACKED BONDS?**

5 A. Yes. Three Ratepayer-Backed Bond transactions illustrate the
6 results that can be achieved by an active and involved commission
7 with an entity focused on ratepayer interests in a joint decision-
8 making relationship in these activities.

9 In 2016, DEF issued Ratepayer-Backed Bonds to recover the costs
10 of its retired nuclear power plant. DEF proposed and negotiated a
11 settlement with the Commission staff and intervenors that allowed its
12 investors to recover the costs of its retired plant and at the same time
13 provide more than \$680 million in net present value benefits to
14 ratepayers. Clearly, a win-win. The capital markets viewed this
15 transaction in a positive manner, further protecting ratepayers from
16 increased capital costs and allowing DEF to raise debt capital in the
17 future at reasonable rates. The markets were especially positive
18 about the net benefits of the transaction's longest maturities, which
19 generally carry the highest rates. The FPSC, DEF, and Saber worked
20 collaboratively, as joint decision-makers on a Bond Team, to make
21 this a success. The FPSC staff and the Florida Office of Public
22 Counsel specifically acknowledged Saber's work on the Bond Team
23 with regards to its development of "best practices" and the excellent

1 pricing of the bonds which yielded significant savings to the Florida
2 ratepayers.

3 In September 2005, Public Service Electric and Gas Company of
4 New Jersey sponsored the issuance of \$102 million of Ratepayer-
5 Backed Bonds. Saber served as financial advisor to the New Jersey
6 Board of Public Utilities (BPU), and Credit Suisse (CS) was the lead
7 underwriter. Normally this transaction might have been difficult to sell
8 because of its small size relative to other competing investments.
9 However, the extensive marketing of those bonds conducted by CS,
10 Barclays and M.R. Beal, with Saber's active participation, led to
11 unprecedented low pricing spreads, despite the disadvantage of
12 relatively small tranche sizes.

13 In December 2005, CenterPoint Energy of Texas initially offered
14 \$1.2 billion of securitized Ratepayer-Backed Bonds to the market.
15 Saber was the independent financial advisor to the PUCT and was,
16 as reflected in the PUCT's Financing Order, granted joint decision-
17 making responsibility with the sponsoring utility. CS was one of the
18 bookrunning Underwriters. In that case, the large size of the
19 transaction, coupled with the timing of the issuance at the end of the
20 year (which traditionally is not a good time to sell securities), posed
21 special challenges. Nevertheless, the Ratepayer-Backed Bonds
22 received worldwide investor demand at record-low credit spreads
23 under market conditions at the time of the offering. The transaction

1 was increased to \$1.85 billion, with over one-third of the bonds being
2 sold to foreign investors. This was the first time a significant portion
3 of an issue of Ratepayer-Backed Bonds ever had been marketed to
4 foreign investors.

5 **Q. THE NORTH CAROLINA SECURITIZATION STATUTE INCLUDES**
6 **A “LOWEST STORM RECOVERY CHARGE” REQUIREMENT. IN**
7 **YOUR VIEW, IS THAT STANDARD APPROPRIATE FOR**
8 **RATEPAYER-BACKED BOND TRANSACTIONS?**

9 A. Absolutely. The proceeds of a bond issuance are cash dollars.
10 Issuers want to raise the maximum amount of dollars at the lowest
11 possible overall cost. Underwriters often have a vested interest in
12 urging the use of a standard of “reasonable cost” because
13 “reasonable” covers a range of outcomes. For any long-term
14 financing, that range might represent millions of dollars in extra costs.
15 One might choose to use a reasonable cost standard to reimburse a
16 doctor, where there are differences in both the type and quality of
17 care. However, there is no reason to pay any more for a bond issue
18 than is necessary especially if the ratepayers are “stuck with bill”.
19 With a “lowest storm recovery charge” standard, the emphasis is on
20 eliminating waste and inefficiency which otherwise might occur under
21 a “reasonable cost” and maximize ratepayer savings by also
22 including the impact of the “time value of money”.

1

STRUCTURING, MARKETING AND PRICING

2

**Q. PLEASE DESCRIBE WHAT IS MEANT BY THE PHRASE
“STRUCTURING, MARKETING AND PRICING” OF RATEPAYER-
BACKED BONDS, AND WHY DOES IT MATTER TO
RATEPAYERS?**

3

4

5

6

A. As described in the testimony of Witnesses Sutherland and Fichera:

7

“Structuring” refers to the legal documentation and the delineation of rights, duties, covenants, responsibilities, and actions of various parties to the transaction under current and anticipated market conditions affecting the bonds and the interaction with investors.

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Structuring also refers to the specific payment schedule for the bonds, the maturity, aggregation of cash flows in tranches (like a series) within the overall maturity, redemption features and the method and frequency of payment.

15

16

17

“Marketing” refers to the communication of the terms, conditions, credit and investment thesis to the Underwriters and potential investors in preparation for pricing.

18

19

20

“Pricing” refers to the actual interest rate and costs assigned to the bonds in exchange for cash. Generally, the bonds are first sold to a group of banks (underwriters) who resell the bonds to investors.

21

Q. THE NORTH CAROLINA STORM RECOVERY BOND STATUTE

22

ENVISIONS THAT THE “STRUCTURING AND PRICING” OF

1 **STORM RECOVERY BONDS WILL ACHIEVE THE “LOWEST**
2 **STORM RECOVERY CHARGES” AT THE TIME THE STORM**
3 **RECOVERY BONDS ARE PRICED. IN YOUR VIEW, SHOULD**
4 **ANY ADDITIONAL ACTIONS BE TAKEN INTO ACCOUNT IN**
5 **DETERMINING WHETHER STORM RECOVERY BONDS**
6 **ACHIEVE THE “LOWEST STORM RECOVERY CHARGES” AT**
7 **THE TIME THE STORM RECOVERY BONDS ARE PRICED?**

8 A. Yes. When commissions in other states have applied a “lowest
9 securitized charges” standard, they often have required to take into
10 account not only decisions related to “structuring and pricing,” but
11 also decisions related to “marketing” the Ratepayer-Backed Bonds.
12 Examples include the 2016 Florida transaction for DEF, the 2007
13 Florida transaction for FPL, the 2007 and 2009 West Virginia
14 transactions for Monongahela Power Company and for The Potomac
15 Edison Company, and the three Texas transactions described in
16 Witness Klein’s testimony. I recommend that the Commission’s
17 Financing Order in this proceeding take into account not only
18 decisions related to “structuring and pricing,” but also decisions
19 related to “marketing” the storm recovery bonds.

20 **Q. IN YOUR VIEW, SHOULD THE “LOWEST STORM RECOVERY**
21 **CHARGE” STANDARD BE APPLIED ONLY BASED ON**
22 **EXPECTATIONS AS OF THE DATE THE FINANCING ORDER IS**
23 **ISSUED, OR SHOULD THE “LOWEST STORM RECOVERY**

1 **CHARGE” STANDARD ALSO BE APPLIED BASED ON ACTUAL**
2 **FACTS THROUGH THE DATE ON WHICH STORM RECOVERY**
3 **BONDS ARE PRICED?**

4 A. In my view, the “lowest storm recovery charge” standard should be
5 applied based on actual facts through the date on which storm
6 recovery bonds are priced.

7 **Q. IN YOUR VIEW, DOES N.C. GEN. STAT. § 62-172 AUTHORIZE**
8 **OR DIRECT THE COMMISSION TO INCLUDE IN ITS STORM**
9 **RECOVERY BOND FINANCING ORDERS A REQUIREMENT**
10 **THAT THE “LOWEST STORM RECOVERY CHARGE”**
11 **STANDARD BE APPLIED BASED ON ACTUAL FACTS**
12 **THROUGH THE DATE ON WHICH STORM RECOVERY BONDS**
13 **ARE PRICED?**

14 A. Yes. This is not among the items specifically required by the statute
15 to be included in storm recovery bond Financing Orders. However,
16 the statute directs that storm recovery bond financing orders are also
17 to include “[a]ny other conditions not otherwise inconsistent with this
18 section that the Commission determines are appropriate.” In my
19 view, it is “appropriate” for the Commission’s Financing Order in this
20 proceeding to include a requirement that the “lowest storm recovery
21 charge” standard be applied based on actual facts through the date
22 on which storm recovery bonds are priced. In addition, for the
23 reasons described above, in my view, it also is appropriate for the

1 Commission's Financing Order in this proceeding to require the
2 "lowest storm recovery charge" determination to take into account
3 not only the "structuring and pricing" but also the "marketing" of storm
4 recovery bonds.

5 **EVALUATION OF JOINT PETITION'S PROPOSED ISSUANCE**
6 **ADVICE LETTER PROCESS**

7 **Q. DOES THE FORM OF FINANCING ORDER PROPOSED BY THE**
8 **COMPANIES JOINT PETITION UNAMBIGUOUSLY REQUIRE**
9 **THAT THE COMPANIES INCLUDE IN THEIR ISSUANCE ADVICE**
10 **LETTERS A "LOWEST STORM RECOVERY CHARGE"**
11 **CONFIRMING CERTIFICATION, BASED ON INFORMATION**
12 **AVAILABLE THROUGH THE DATE ON WHICH STORM**
13 **RECOVERY BONDS ARE PRICED?**

14 A. I believe the proposed form of Financing Order is ambiguous as to
15 whether the Companies' Issuance Advice Letters must include a
16 "lowest storm recovery charge" confirming certification, based on
17 information available through the date on which storm recovery
18 bonds are priced.

19 On the one hand, Finding of Fact 33 in the proposed form of
20 Financing Order states:

21 Because the actual structure and pricing of the Storm
22 Recovery Bonds are unknown as of the issuance of this
23 Financing Order, following determination of the final
24 terms of the Storm Recovery Bonds and before
25 issuance of the Storm Recovery Bonds, DEP will file

1 with the Commission for each series of Storm
 2 Recovery Bonds, an IAL, as well as a form of True-Up
 3 Adjustment Letter¹⁴ (“TUAL,” and together with the
 4 IAL, the “IAL/TUAL”) in the forms attached hereto as
 5 Appendices B and C. The initial Storm Recovery
 6 Charges and the final terms of the Storm Recovery
 7 Bonds described in the IAL/TUAL will be final unless
 8 before noon on the third business day after pricing the
 9 Commission issues an order finding that the proposed
 10 issuance does not comply with the Standards of this
 11 Financing Order in this Finding of Fact No. 33. The
 12 “Standards of this Financing Order” are: . . . 7) the
 13 structuring and pricing of the Storm Recovery Bonds,
 14 including the issuance of SRB Securities, resulted in
 15 the lowest Storm Recovery Charges consistent with
 16 market conditions at the time the Storm Recovery
 17 Bonds are priced and the terms set forth in this
 18 Financing Order.

19 The form of Issuance Advice Letter attached as Appendix C to the
 20 form of Financing Order attached as Exhibit C to the Joint Petition
 21 states:

22 The Financing Order requires the Company to confirm,
 23 using the methodology approved therein, that the
 24 actual terms of the SRB Notes and Storm Recovery
 25 Bonds result in compliance with the standards set forth
 26 in the Financing Order. These standards are:

27 * * *

28 7. the structuring and pricing of the Storm
 29 Recovery Bonds, including the issuance of SRB Notes,
 30 resulted in the lowest Storm Recovery Charges
 31 consistent with market conditions at the time the Storm
 32 Recovery Bonds are priced and the terms set forth in
 33 this Financing Order.

34 The form of Company Certification included as Attachment 8 to
 35 Appendix C states:

36 Based on the statutory criteria and procedures, the
 37 record in this proceeding, and other provisions of this

1 Financing Order, DEP certifies the statutory
2 requirements for issuance of a financing order and
3 Storm Recovery Bonds have been met, specifically
4 that the issuance of the SRB Notes and underlying
5 Storm Recovery Bonds on behalf of DEP and the
6 imposition and collecting of storm recovery charges
7 authorized by this Financing Order provide quantifiable
8 benefits to customers of DEP as compared to the costs
9 that would have been incurred absent the issuance of
10 Storm Recovery Bonds and that the structuring and
11 pricing of the SRB Notes and underlying Storm
12 Recovery Bonds issued on behalf of DEP result in the
13 lowest storm recovery charges payable by the
14 customers of DEP consistent with market conditions at
15 the time such SRB Notes and underlying Storm
16 Recovery Bonds are priced and the terms set forth in
17 the Financing Order.

18 On the other hand, page 56 of the proposed form of Financing Order
19 states: “Finally, the combined IAL/TUAL shall include certifications
20 from DEP, **if required**, that the structuring and pricing of the Storm
21 Recovery Bonds achieved the **Statutory Cost Objectives.**”
22 Similarly, Finding of Fact 11 states: “Finally, the combined IAL/TUAL
23 shall include certifications from DEP **if required**, that the structuring,
24 pricing and Financing Costs of the Storm Recovery Bonds achieved
25 the **Statutory Cost Objectives.**” (emphasis added) This language
26 suggests that these confirming certifications from DECF and DEP
27 might not be required.

28 In addition, page 9 of the proposed form of Financing Order defines
29 “Statutory Cost Objectives” to mean, collectively: “(i) the proposed
30 issuance of Storm Recovery Bonds and the imposition of Storm
31 Recovery Charges will provide quantifiable benefits to customers as

1 compared to the costs that would have been incurred absent the
2 issuance of Storm Recovery Bonds and (ii) the structuring and
3 pricing of the Storm Recovery Bonds are **reasonably expected** to
4 result in the lowest Storm Recovery Charges consistent with market
5 conditions at the time the Storm Recovery Bonds are priced and the
6 terms set forth in this Financing Order.” (emphasis added). This
7 language suggests that any required confirming certifications from
8 the Companies might be based on their reasonable expectations as
9 of the date of the Financing Order, rather than on information
10 available through the date on which Storm Recovery Bonds are
11 priced.

12 I recommend that the language on page 9, in Finding of Fact 11, and
13 on page 56 be revised to be clear in requiring that the Companies
14 include in their Issuance Advice Letters a “lowest storm recovery
15 charge” confirming certification, based on information available
16 through the date on which storm recovery bonds are priced.

17 **Q. ARE UNDERWRITERS AND INVESTORS COOPERATIVE IN**
18 **ACHIEVING THE LOWEST SECURITIZED CHARGES?**

19 A. It varies. Some are more cooperative than others. Fundamentally,
20 Underwriters have an inherent conflict of interest in determining the
21 price of the bonds for issuers. Underwriters by definition, will be the
22 initial purchasers of the bonds, generally purchasing the bonds from
23 the issuer at an agreed discount and then reselling the bonds to

1 investors at face value. The higher the interest rate, the easier it will
2 be for the Underwriters to resell the bonds at face value. Therefore,
3 it is in the Underwriters' economic interest to get a higher interest
4 rate to make it easier to induce their customers, the investors, to buy
5 the bonds. Investors also want as high an interest rate as possible.

6 **Q. DOES ATTEMPTING TO ACHIEVE A LOWEST SECURITIZATION**
7 **CHARGE STANDARD SOMETIMES CREATE MORE COSTS FOR**
8 **RATEPAYERS IN CERTAIN RESPECTS?**

9 A. No. Pursuing a lowest Securitization charge standard might require
10 transaction participants to work harder, and possibly a bit longer, but
11 not necessarily at a higher net economic cost. Working harder for the
12 ratepayer saves money. Among the on-going transaction costs, the
13 greatest economic cost to ratepayers is the interest rate on the bonds
14 which ratepayers will be paying for up to 15-20 years or more. This
15 dwarfs most of the up-front issuance expenses.

16 The approval standard utilized by the Commission in this type of
17 transaction with its very significant costs, needs to be a much
18 stronger standard than "reasonable cost." Because the incentives
19 between the utility and ratepayer are not clearly aligned, and full
20 after-the-fact prudency reviews are not possible, the Commission's
21 standard should be "lowest storm recovery charge" and maximum
22 present value savings for ratepayers. Without involvement in real
23 time by Public Staff and its advisor's expertise, there will be no way

1 for the Commission to have confidence that the transaction was
2 priced at the lowest interest rate possible under then-current market
3 conditions. Every dollar of costs in this Ratepayer-Backed Bond
4 transaction is a ratepayer dollar. There is no material risk to the
5 utilities' shareholders given the robust true-up mechanism combined
6 with the state pledge of non-interference.

7 This is one reason why extra care needs to be taken, in cooperation
8 with the Companies, in selecting experienced and responsive
9 transaction participants. It is essential to put together a team which
10 shares similar objectives and a commitment to excellence, which can
11 provide economies of scale, and which is responsive to competitive
12 pressures and economic incentives. This will build investor
13 confidence in the bond offering and customer confidence in the final
14 decision made by the Commission to allow the bond offering to
15 proceed using the issuance advice letter process.

16 **BENEFITS OF PUBLIC STAFF AND AN INDEPENDENT**
17 **FINANCIAL ADVISOR**

18 **Q. HOW WILL ACTIVE INVOLVEMENT OF THE COMMISSION AND**
19 **THE PUBLIC STAFF WITH ITS FINANCIAL ADVISOR IN THE**
20 **STRUCTURING, MARKETING, AND PRICING OF THESE**
21 **RATEPAYER-BACKED BONDS AFTER ISSUANCE OF THE**
22 **FINANCING ORDER ENSURE A "LOWEST STORM RECOVERY**

1 **CHARGE” TRANSACTION UNDER MARKET CONDITIONS AT**
2 **THE TIME OF PRICING?**

3 A. Because the Financing Order will be irrevocable, the interests of
4 ratepayers need to be fully represented with proper economic
5 incentives at every step of the process. The Companies and their
6 agents have specific interests in the outcome of this transaction: to
7 raise the full authorized amount in the shortest time possible and with
8 the least possible effort. Those interests might diverge in some
9 material respects from the interests of ratepayers who will bear the
10 full economic burden of the transaction for 15-20 years or more.
11 Nevertheless, a cooperative and collaborative effort can achieve
12 common goals.

13 In this case, many decisions affecting ratepayer costs and risks
14 cannot be known until after a financing order has been issued. The
15 Companies have proposed a process that would provide important
16 information to the Commission only by the issuance of advice letters,
17 delivered after the structuring, marketing and pricing process is
18 complete. This is inadequate for the Commission to make an
19 informed decision. Without having been at the “negotiating table” in
20 the first instance, it is impossible to have adequate information to
21 make an informed decision to either stop or let the transaction
22 proceed with full confidence that all appropriate efforts have been
23 undertaken. “At the negotiating table” is different from being outside

1 the room and getting reports and information from the utility on its
2 discussions after the fact.

3 As discussed above in this testimony, Underwriters who will provide
4 much of the market information concerning the upcoming sale of the
5 securitized storm recovery bonds will have no fiduciary obligation to
6 DEC/DEP, the Commission, or ratepayers. They do not have to work
7 in the best interests of the ratepayers and are permitted to act in their
8 own financial interest. It is evident in the standard underwriting
9 agreement used in these and other transactions which explicitly
10 states that there is no fiduciary relationship and often states that any
11 review by the Underwriters of the transaction will be performed solely
12 for the benefit of the Underwriters and shall not be on behalf of the
13 Issuer or utility. (See also the testimony of Witness Brian Maher on
14 the issue of fiduciary obligation.)

15 Only by having the Commission and the Public Staff and its financial
16 advisor involved at every step after issuance of the Financing Order,
17 and by working together with the Companies as joint decision makers
18 during all critical stages, can we ensure that the lowest storm
19 recovery charges to ratepayers is achieved.

20 **Q. CAN YOU EXPAND ON WHY IT IS NECESSARY FOR THE**
21 **COMMISSION TO ENSURE THE CONTINUING ACTIVE**
22 **INVOLVEMENT OF PUBLIC STAFF AND ITS FINANCIAL**
23 **ADVISOR AFTER ISSUANCE OF THE FINANCING ORDER?**

1 A. Yes. Both the Commission, Public Staff and their respective staffs
2 have many years of experience in reviewing and approving the
3 issuance of traditional utility debt and equity securities. Generally,
4 regulatory Commissions and ratepayer advocates do not have
5 experience in reviewing and approving securitized Ratepayer-
6 Backed Bonds where the utility may have little or no incentive to
7 minimize the rate of interest or the costs of issuance, or to offer
8 reasonable representations, warranties and covenants for the
9 benefit of ratepayers. In this case, as specifically authorized by N.C.
10 Gen. Stat. § 62-172(n), Public Staff has decided to supplement its
11 experience with that of an experienced and independent financial
12 advisor.

13 The Companies, as well, have little or no experience in issuing
14 securitized Ratepayer-Backed Bonds. Their sister utility, DEF, has
15 done one transaction. This heightens the benefits of a continuing and
16 collaborative process with the Commission, Public Staff and its
17 experienced financial advisor after the financing order is issued.
18 Moreover, Witness Heath has testified that the Companies financial
19 advisors have no fiduciary relationship with the Companies, so it is
20 more difficult to evaluate the advice and information given about a
21 subject with which they are not generally familiar, and about which
22 their financial advisors may be conflicted.

1 With the help of experts intimately familiar with the legal and financial
2 specifics and nuances of Ratepayer-Backed Bonds, and with a
3 fiduciary duty to the Commission, Public Staff, and ratepayers, the
4 Commission can ensure that ratepayers' interests are protected and
5 that the Companies receive the proceeds of a successful offering. An
6 actively involved and independent financial advisor to the
7 Commission or to Public Staff, who has an implicit fiduciary
8 relationship with the Commission, will add tremendously to the
9 Commission's ability to reach this goal.

10 For example, corporations and financial advisory firms interface
11 regularly with public capital markets, whereas utility commissions
12 and Public Staff do not. Public Staff's financial advisor for the
13 proposed storm recovery bonds, Saber Partners, is intimately
14 familiar with the structuring, marketing, and pricing of Ratepayer-
15 Backed Bonds, as well as with the participants in the corporate,
16 asset-backed securities and international securities markets. Saber
17 Partners will be able to provide critical information and perspective
18 to the Commission to discharge its duties and to assist the
19 Companies.

20 **NEED FOR INDEPENDENT ANALYSIS AND**
21 **FINANCIAL OPINIONS**

22 **Q. BASED ON YOUR EXPERIENCE, WHY SHOULD THE**
23 **COMMISSION NOT SIMPLY RELY ON THE "ISSUANCE ADVICE**

1 **LETTER” INCLUDING THE CERTIFICATION FROM THE**
2 **COMPANIES THAT THE PRICING OF THE STORM RECOVERY**
3 **BONDS RESULTED IN THE LOWEST STORM RECOVERY**
4 **CHARGE, AND WHY IS THAT NOT SUFFICIENT AS AN**
5 **INDICATOR OF A SUCCESSFUL TRANSACTION?**

6 A. From my perspective, issuance advice letters may not always be
7 conflict free. As I described above, there is an inherent conflict of
8 interest on the part of utility and Underwriters in pricing any bonds.
9 Based upon my experience as the Treasurer of a very large utility, I
10 realized very quickly that Underwriters of our debt issuances weren’t
11 necessarily “on the same page” as we, the issuers, were. We shared
12 many of the same goals concerning the execution of an efficient
13 transaction, but the Underwriters’ desire to maximize profits for
14 themselves and investors were not always in line with our goals as
15 issuer.

16 In fact, underwriting agreements clearly state that the Underwriters
17 do not have a fiduciary responsibility in these types of transaction.
18 Witness Brian Maher of Saber delineates this issue extensively in his
19 testimony.

20 From my work experience, an analogy comes to mind which strongly
21 resembles the issue at hand. For decades, “Fairness Opinions” have
22 played an integral part in merger and acquisition (M&A) transactions.

23 A Fairness Opinion is a letter summarizing an analysis prepared by

1 an investment bank or an independent financial third party, which
2 indicates whether certain financial elements in a transaction, such as
3 price, are fair to a specific constituent. These opinions often are
4 issued to assist the Board of Directors in assessing the
5 appropriateness of an M&A transaction so they can fulfill their
6 fiduciary duty to shareholders. The Fairness Opinion does not
7 include a recommendation on whether the Board should approve the
8 transaction. Rather, it helps the Board build a record that it has
9 satisfied its fiduciary duty of care in reviewing the transaction.

10 However, these Fairness Opinions are not without controversy. A
11 principal objection is that the Fairness Opinion often is provided by
12 the same party that is advising the buyer (or target) for a fee that is
13 contingent on the successful completion of the deal. This represents
14 a clear conflict of interest and a potential lack of objectivity.

15 In a typical M&A transaction, both the buyer and target will each
16 arrange for the delivery of their own separate Fairness Opinions. This
17 does not necessarily solve the conflict of interest conundrum. These
18 Fairness Opinions have come under greater scrutiny and litigation in
19 recent years as almost half of very large M&A transactions have
20 been challenged.

21 While at Con Edison of New York, I was intimately involved in a
22 potential acquisition of a neighboring utility. Con Ed, as buyer, and
23 the target utility obtained Fairness Opinions from our respective

1 investment bankers and announced the transaction. Con Ed then
2 hired, albeit a little late, an independent financial adviser to evaluate
3 certain risks relating to the competitive energy marketplace. The
4 advisor identified some significant risks in the target company's
5 energy portfolio which had not been delineated in the Fairness
6 Opinions and which Con Ed was not willing to accept. As a result,
7 the transaction was cancelled, which later resulted in years of
8 litigation.

9 The independent financial advisor "saved the day," by recognizing
10 risks that the conflicted investment bankers did not.

11 That is why it is important for stakeholders, like ratepayers in this
12 transaction, to have an independent financial advisor whose opinions
13 and analyses are based on experience and knowledge of the
14 intricacies of the transaction and market.

15 **Q. IF INVESTORS ARE MOST FAMILIAR WITH TRADITIONAL**
16 **UTILITY BONDS AND ARE LIKELY TO COMPARE THESE**
17 **STORM RECOVERY BONDS TO THOSE SECURITIES, WITH**
18 **RESPECT TO LEGAL CHARACTERISTICS, HOW DO STORM**
19 **RECOVERY RATEPAYER-BACKED BONDS COMPARE TO**
20 **TRADITIONAL UTILITY BONDS?**

21 A. The securitized storm recovery utility bonds themselves are simple
22 and straightforward. As most commonly structured, they are carried
23 as obligations of the consolidated entity for accounting and tax

1 purposes, much like conventional corporate securities. However, the
2 structure of the SPE issuer and the administration of the collateral
3 supporting Ratepayer-Backed Bonds require extensive
4 documentation. For example, Ratepayer-Backed Bonds require a
5 Sale Agreement, Servicing Agreement, Administration Agreement,
6 special tax, bankruptcy, and other legal opinions, and must meet
7 other requirements of the rating agencies for a “AAA” rating.

8 **Q. GIVEN THAT THERE HAS BEEN ABOUT \$50 BILLION OF**
9 **RATEPAYER-BACKED BONDS SOLD OVER THE LAST 20**
10 **YEARS, AT ANY TIME, ISN'T THERE AN EASILY IDENTIFIABLE**
11 **RATE FOR ALL RATEPAYER-BACKED BONDS WITH THE**
12 **SAME SCHEDULED MATURITY?**

13 A. No. First of all, less than \$5 billion of the \$50 billion issued, are still
14 outstanding. Second, and perhaps more important, the Ratepayer-
15 Backed Bonds have been re-sold infrequently. This means that in
16 rapidly changing and dynamic markets there is not a focus on these
17 bonds. Moreover, since the credit crisis of 2008-09, there has been
18 a tremendous amount of turnover among investors, Underwriters,
19 and market makers.

20 Though many discussions with Underwriters defer pricing decisions
21 to “the market,” there is no simple way to assess the interest rate for
22 the bonds of any issuer, particularly an infrequent issuer that is
23 forced to sell into the market. Some assert that there is a known rate

1 (spread/yield) for new issue bonds based on the “market” where
2 Ratepayer-Backed Bonds are currently traded in the secondary
3 market. The problems with this argument are manifold:

- 4 1. There is no active daily trading of Ratepayer-Backed Bonds.
- 5 2. Secondary market prices and amounts are often small odd
6 lots that carry widely differing dollar prices, all of which affect
7 direct comparisons to par priced issues.
- 8 3. New issuances of Ratepayer-Backed Bonds have been
9 sporadic and infrequent, and marketing efforts have varied
10 widely. Thus, there is not a constant flow of new issue pricing
11 information to establish any consistent benchmark.

12 An efficient market matches a willing buyer and willing seller, each
13 having access to all information that is material to the investment
14 decision. So, when we get to the basics, it is a matter of negotiation,
15 marketing, and selling even in a competitive bidding situation. The
16 price of your house is not solely a function of the price of other
17 houses for sale. No two houses are identical. It is a function of a
18 range of factors affecting perception concerning quality, replacement
19 value and other factors, including the needs of specific buyers. The
20 same principles apply to the marketing of ratepayer-backed bonds.

1 **GETTING THE MOST VALUE FROM UNDERWRITERS AND**
2 **INVESTORS FROM A TOP CREDIT RATING**

3 **Q. AREN'T ALL SECURITIES THAT HAVE THE SAME MATURITY**
4 **AND IDENTICAL "AAA" RATINGS PRICE THE SAME SO THERE**
5 **IS VERY LITTLE NEED TO PROTECT RATEPAYER INTERESTS?**

6 A. No. As described in Witness Sutherland's testimony, there are wide
7 discrepancies in pricing between and among securities of the same
8 rating, even within the Ratepayer-Backed Bond market segment.
9 These discrepancies exist in both the market for new issuances and
10 in the secondary market for prior issuances, and they are particularly
11 acute for first-time issuers of Ratepayer-Backed Bonds. This is called
12 "relative value" of the security.

13 **Q. WOULD APPEALING TO A CERTAIN TYPE OF AN INVESTOR**
14 **SEGMENT AFFECT THE COST OF STORM RECOVERY BONDS**
15 **AND THEREFORE RATEPAYER COSTS?**

16 A. Yes. As described in the testimony of Witness Maher, appealing to
17 the appropriate investor segment creates the baseline by which
18 investors value the security and determine the interest rate they will
19 accept to hold the Ratepayer-Backed Bonds.

20 For example, an investor who wishes to make a quick profit in trading
21 the security (also known as a "Flipper") might be on the prowl for
22 bonds that are likely to be over-subscribed in the initial offering, with
23 a view to immediately re-selling the bonds at a higher price to other

1 investors who placed unfilled orders at the initial offering price.
2 Targeting investors who are very worried about maintaining their
3 principal for the long-term and who do not expect to sell the bonds in
4 the near future (the “Buy and Hold” investor) may accept a lower
5 interest rate because those investors are more concerned about
6 long-term risk than a quick profit. Foreign investors who want safety
7 in U.S. dollars (e.g., investors from China) may also be willing to
8 accept lower yields than U.S. domestic hedge fund managers who
9 have high yielding targets for their investment portfolio to keep
10 attracting capital inflows to their funds.

11 Furthermore, appealing to the broadest possible base of investors,
12 rather than targeting a small group of large accounts, will create
13 greater competition. Large investor accounts often believe they have
14 “market power” and therefore can demand higher yields for quick
15 execution with their capital. Although Underwriters are sometimes
16 willing to oblige them, competition with other Underwriters and
17 investors can drive the market to lower costs.

18 **Q. HOW SHOULD RATEPAYER-BACKED BONDS BE PRICED IF**
19 **THE MARKETS WERE EFFICIENT AND THE RELATIVE VALUE**
20 **OF THE BONDS FULLY UNDERSTOOD?**

21 A. If the Ratepayer-Backed Bonds are properly structured as corporate
22 securities and not asset-backed securities, as described in Witness
23 Sutherland’s testimony about the MP Funding, PE Funding, and

1 Duke Energy Florida Project Finance bonds, then they will appeal to
2 the large and diverse corporate bond market and not the more limited
3 asset-backed securities market. For example, the Barclays (now
4 Bloomberg-Barclays) bond indexing service for the first time included
5 the 2016 DEF ratepayer-backed bonds in their Corporate Utility Bond
6 Index (see HS EXHIBIT A, Barclays Technical Note: Classification of
7 Duke Energy Florida Project Finance, LLC Bonds). Many investors
8 use this index to judge the performance of their portfolios, so this
9 vastly expands the market since many of these investors must buy
10 the index. The financial press noted this important development in
11 June 2016. (See Schoenblum Exhibit 2, Asset Securitization Report,
12 Duke Utility Fee Securitization Sets Important Precedent, June 21,
13 2016.) The bonds achieved record low interest rates and credit
14 spreads for long-term Ratepayer-Backed Bonds.

15 In an efficient market where all potential investors are properly
16 educated on the relative value of Ratepayer-Backed Bonds versus
17 market comparables, Ratepayer-Backed Bonds would likely be
18 priced like U.S. agency securities or other top corporate AAA rate
19 bonds, like Johnson & Johnson, as the 2016 DEF Ratepayer-Backed
20 Bonds did. We would expect storm recovery bonds issued forth
21 Companies to achieve similar results if properly structured and
22 marketed.

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SUMMARY OF A BEST PRACTICES APPROACH

Q. PLEASE SUMMARIZE THE SPECIFIC STEPS OF THE BEST PRACTICES APPROACH FOR THE COMMISSION IN THE STORM RECOVERY BOND ISSUANCE PROCESS.

A. The Commission should:

1. Participate in the selection of underwriters, legal counsel, and other transaction participants and in defining the responsibilities of each to the extent that each is to be paid directly or indirectly from storm recovery bond proceeds or from the storm recovery charge collections. To assist it in implementing its authority, the Commission, or its designee, should act by and through its staff, the Public Staff, and their experts to serve as joint-decision maker with the applicant utilities in all matters related to the structuring, marketing and pricing of the proposed storm recovery bonds. The experts the Commission relies upon should have a duty solely to protect ratepayers and be free of any conflicts of interests with the utility, underwriters or investors.¹

¹ See Wisconsin PSC's 2004 Financing Order issued to Wisconsin Electric Power Company (Docket 6630-ET-100), Ordering Paragraph 7 ("The Commission shall oversee all negotiations regarding the structuring, marketing, and pricing of the environmental trust bonds and, without limitation, the selection of underwriter(s), counsel, trustee(s) and other parties necessary to the transaction and to review and approve the terms of all transaction documents.")

- 1 2. Reduce risks borne by ratepayers through careful review and
 2 negotiation of all transaction documents and contracts that
 3 could affect future ratepayer costs.
- 4 3. Ensure that all statutory limits which benefit ratepayers are
 5 strictly enforced.
- 6 4. Establish procedures to ensure that all savings are allocated
 7 or transferred to ratepayers.²
- 8 5. Require that the storm recovery bonds be offered to the
 9 broadest market possible to expand the market to garner

² See the California PUC's 2004 Financing Order issued to PG&E (Decision 04-11-015 November 19, 2004), pages 40 and 41 ("To the extent PG&E's incremental costs to provide this service are less than the servicing fee revenue from the Bond Trustee, PG&E will return that excess revenue to consumers through the ERBBA."); New Jersey BPU's 2005 Financing Order issued to PSE&G (BPU Docket No. EF03070532), Ordering Paragraph 22 ("However, if the Servicing Fee is greater than the actual incremental costs to service the BGS Transition Property, other rates of the Petitioner shall be adjusted to reflect the difference between actual servicing costs and the Servicing Fee."); Montana PSC's 1998 Financing Order issued to Montana Power (Docket No. D97.11.219; Order No. 6035a), pages 6 and 7 ("The full amount of the market-based servicing fee will be included in the FTA charges. However, as long as Applicant is servicer, Applicant proposes a ratemaking mechanism that will provide a credit to ratepayers equal in value to any amounts it receives as compensation, since these servicing costs will generally be included in the Applicant's overall cost of service."); California PUC's 1997 and 1998 Financing Orders issued to PG&E (Decision 97-09-055 September 3, 1997), SCE (Decision 97-09-056 September 3, 1997), SDG&E (Decision 97-09-057 September 3, 1997) and Sierra Pacific (Decision 98-10-021 June 24, 1998), page 6 ("The full amount of the market-based servicing fee will be included in the FTA charges. However, as long as PG&E is servicer, PG&E proposes a ratemaking mechanism which will provide a credit, after the rate-freeze period, to residential and small commercial ratepayers in PG&E's Rate Reduction Bonds Memorandum Account equal in value to any amounts it receives as compensation, excepting only amounts needed to cover incremental, out-of-pocket costs and expenses incurred by PG&E to service the RRBs. These types of expenses would include required audits related to PG&E's role as servicer, and legal and accounting fees related to the servicing obligation. Thus, the only net ratemaking impact will be such incremental expenses.").

- 1 lower interest rates for the benefit of ratepayers through
 2 increased competition.³
- 3 6. Require transparency in the distribution, in the initial pricing
 4 and in the secondary market for the storm recovery bonds to
 5 support the integrity of the process.
- 6 7. Direct the Commission's staff and the Public Staff and its
 7 independent financial advisor to take part fully and in advance
 8 in all aspects of structuring, marketing, and pricing the storm
 9 recovery bonds, and direct the financial advisor to disapprove
 10 any decision that would not result in the lowest all-in cost of
 11 funds and the lowest storm recovery charges to ratepayers.⁴
- 12 This should include:

³ In support of this best practice, it will be useful for the financing order to include a variety of findings, including (a) each SPE is responsible to the Commission in connection with its issuance of storm-recovery bonds; (b) storm-recovery property is not a receivable; (c) the State Pledge and the automatic true-up adjustment mechanism constitute a State of Florida guarantee of regulatory action to ensure payment of principal and interest on the storm-recovery bonds (see e.g., Wisconsin PSC 2004 Financing Order issued to Wisconsin Electric (Docket 6630-ET-100), Ordering Paragraph 1: "The approval of this Financing Order, including the true-up provisions, by the Commission constitutes a guarantee of state regulatory action to ensure repayment of the environmental trust bonds and associated costs."; California PUC 2004 Financing Order issued to PG&E (Decision 04-11-015 November 19, 2004), Ordering Paragraph 40: "All true-up adjustments to the DRC shall guarantee the billing of DRC charges necessary to generate the collection of amounts sufficient to make timely provision for all scheduled (or legally due) payments . . ."); and (d) if all private consumers of electricity in FPL's service area cease to consume electricity and/or fail to pay storm-recovery charges, the automatic true-up adjustment mechanism will cause state and local governments in FPL's service area to be payors of last resort.

⁴ See Ordering Paragraph 26 of the Texas PUC's 2005 Financing Order issued to CenterPoint PUC Docket No. 30485); Ordering Paragraph 21 of the Texas PUC's 2002 Financing Order issued to Central Power & Light (Docket 21528); Ordering Paragraph 21 of the Texas PUC's 2002 Financing Order issued to TXU Electric (Docket No. 21528); Ordering Paragraph 21 of the Texas PUC's 2002 Financing Order issued to Reliant Energy (Docket No. 21665); Ordering Paragraph 17 of the New Jersey BPU's 2005 Financing

- 1 a. Reviewing, analyzing, and proposing revisions to all
2 documentation to better protect ratepayers, including
3 specific certifications, representations, indemnities,
4 and warranties, therefore protecting against higher
5 (and hidden) post-transaction ratepayer costs;
- 6 b. Evaluating the performance of underwriters of prior
7 Ratepayer-Backed Bonds;⁵ include in any offering or
8 bidding syndicate one or more underwriters without
9 prior relationships with the Companies or their affiliates
10 (prior relationships can entail conflicts of interest); tie
11 any negotiated Underwriter compensation to
12 performance—actual storm recovery bond sales at
13 lower cost to ratepayers—to create competition within
14 the underwriting syndicate and promote lowest cost;⁶

Order issued to PSE&G (BPU Docket No. EF03070532); Ordering Paragraph 7 of the Wisconsin PSC's 2004 Financing Order issued to Wisconsin Electric Power Company (Docket 6630-ET-100).

⁵ See Ordering Paragraph 26 of the Texas PUC's 2005 Financing Order issued to CenterPoint PUC Docket No. 30485); Ordering Paragraph 21 of the Texas PUC's 2002 Financing Order issued to Central Power & Light; Ordering Paragraph 21 of the Texas PUC's 2002 Financing Order issued to TXU Electric (Docket No. 21528); Ordering Paragraph 21 of the Texas PUC's 2002 Financing Order issued to Reliant Energy (Docket No. 21665); Ordering Paragraph 17 of the New Jersey BPU's 2005 Financing Order issued to PSE&G (BPU Docket No. EF03070532); Ordering Paragraph 7 of the Wisconsin PSC's 2004 Financing Order issued to Wisconsin Electric (Docket 6630-ET-100).

⁶ See Texas PUC's 2005 Financing Order issued to CenterPoint (PUC Docket No. 30485), Finding of Fact 110: "The Commission's financial advisor or designated representative shall require a certificate from the bookrunning underwriter(s) confirming that the structuring, marketing, and pricing of the transition bonds resulted in the lowest transition bond charges consistent with market conditions and the terms of this financing order." See also Wisconsin PSC's 2004 Financing Order issued to Wisconsin Electric Power Company (Docket 6630-ET-100), Ordering Paragraph 37: "Following determination of the final terms

- 1 c. If a negotiated underwriting process is selected,
2 underwriters need to develop a written marketing plan
3 well in advance of actually entering the market. The
4 written plan should implement robust marketing efforts
5 tailored to the unique strengths of the storm recovery
6 bonds, emphasizing the need to broaden distribution
7 and to attract non-traditional investors, and rejecting
8 Underwriters' plans that focus solely on selling storm
9 recovery bonds to previous ratepayer-backed bond
10 investors;
- 11 d. Continually analyze market developments and
12 transactions to adopt successful techniques and utilize
13 them in new issuance(s); and
- 14 e. "Trust but Verify": require Underwriters to document
15 and support their marketing efforts and pricing
16 recommendations to ensure their full attention and
17 focus on accuracy and due diligence, thereby fostering
18 aggressive pricing.
- 19 8. Require fully accountable certifications from the bookrunning
20 underwriter(s), the Companies and the Public Staff's financial
21 advisor as to actions taken to achieve the lowest cost of funds

of each series of environmental trust bonds and prior to issuance of the environmental trust bonds, the Commission may require any certificates from the Applicant's underwriters."

1 and the lowest storm recovery charges under market
2 conditions at the time of pricing.

3 9. Provide that the Commission has authority to enforce the
4 provisions of the Financing Order, the Servicing Agreement,
5 the Sale Agreement, the Indenture, and other transaction
6 documents for the benefit of the ratepayers.⁷

7 **Q. DOES THAT CONCLUDE YOUR TESTIMONY?**

8 A. Yes.

⁷ See e.g., Wisconsin PSC's 2004 Financing Order issued to Wisconsin Electric Power Company (Docket 6630-ET-100), Ordering Paragraph 17 ("The Commission, acting on its own behalf or through the Attorney General, may enforce this Financing Order and related transaction documents, including those contemplated by the Affiliated Interest Final Decision, for the benefit of Wisconsin ratepayers to the extent permitted by law including, the enforcement of any ratepayer indemnification provisions in connection with specified items in the servicing agreement.")

1 Q. And, Mr. Schoenblum, do you have a summary
2 you'd like to provide?

3 A. Yes.

4 Q. Please proceed.

5 A. Good morning. I am a senior advisor to Saber
6 Partners, LLC. Saber is an independent financial
7 advisor to the Public Staff in the proceeding regarding
8 the issuance of storm recovery bonds by Duke Energy
9 Carolinas and Duke Energy Progress.

10 I have 35 years of utility financial
11 experience. I was employed by the Consolidated Edison
12 Company of New York, or Con Ed, in various senior
13 financial capacities such as treasurer, controller, and
14 vice president of strategic planning. I was also a key
15 member of the investor relations team and met regularly
16 with investors and bankers. I testified in numerous
17 rate cases as well as proceedings relating to M&A
18 transactions initiated by Con Ed.

19 With regards to ratepayer-backed bonds, I
20 submitted direct testimony in 2015 in the Duke Energy
21 Florida \$1.3 billion transaction which refinanced the
22 unrecovered costs of a nuclear power plant. In 2018, I
23 submitted testimony in a California proceeding
24 regarding the risks and benefits of securitization.

1 My testimony in this proceeding addresses
2 three major issues. One, the need for Commission and
3 Public Staff involvement in all aspects of the issuance
4 of Ratepayer-Backed Bonds; number 2, differences
5 between incentives that exist for standard utility bond
6 issuances versus Ratepayer-Backed Bonds; number three,
7 the need for a fiduciary relationship between the
8 various participants in the issuance of
9 Ratepayer-Backed Bonds.

10 Commission Involvement. I believe that all
11 parties involved in the issuance of these
12 Ratepayer-Backed Bonds should work collaboratively in a
13 cooperative fashion to structure the transaction. This
14 will ensure that investors and ratepayers that their
15 interests are being protected and will produce a
16 successful transaction with the greatest economic
17 benefit. Since ratepayers are effectively the ones who
18 will repay the debt to bondholders, the Commission must
19 ensure that their interests are best served through
20 enhanced regulatory oversight.

21 The most efficient manner to achieve these
22 goals is through a bond team that includes all
23 participants, including the Public Staff, its
24 independent financial advisor, and the Commission.

1 This approach worked very effectively in the
2 above-mentioned DEF transaction which was praised by
3 the markets and the Florida Commission staff as being
4 an efficient process yielding superior results. It
5 also worked well in other states, as delineated in my
6 testimony. My motto is "Why tamper with success?"

7 Differing Incentives. As a former treasurer,
8 I can attest to the regulatory incentives that standard
9 utility debt issuances have. I was always worried that
10 the New York Commission would second-guess Con Ed's
11 marketing or pricing in future rate proceedings. Thus,
12 we were extremely careful that we should not be exposed
13 to such potential oversight, both in terms of interest
14 rates and fees paid to underwriters. Ratepayer-Backed
15 Bonds do not have these regulatory incentives. The
16 North Carolina Utility Commission cannot second-guess
17 the most important aspects of the storm recovery bond
18 transaction in future rate proceedings. The State has
19 pledged not to interfere. Recovery of issuance costs
20 and interest costs are guaranteed. The True-up ensures
21 full cost recovery.

22 As such, it is extremely important that we
23 get it right the first time. The issuance needs to be
24 handled in an efficient manner, yielding the lowest

1 cost possible. Adopting the best practices recommended
2 by Saber and having all parties work in a collaborative
3 manner will, in my opinion, create the appropriate
4 incentives for a successful transaction. My testimony
5 lists several states that have adopted these best
6 practices in their financing orders. I recommend the
7 same in the instant proceeding.

8 Fiduciary Relationship. I concur with
9 witness Maher that the various parties to this
10 transaction should have a fiduciary relationship with
11 either the utilities or the Commission. That entails
12 that the Companies and the Commission need to receive
13 conflict-free advice from the experts. The parties
14 need to ensure that conflicts of interest are avoided.
15 For example, utilizing an underwriter to also provide
16 consulting advice might yield a conflict, even though
17 Witness Heath believes that structuring advisors,
18 quote, are often in the best position, close quote, to
19 be the lead underwriter.

20 Lastly, it is my opinion that the form of
21 issuance advice letters, IAL, outlined in the proposed
22 financing order filed by the Companies, needs to be
23 strengthened to include certification that the
24 structuring, marketing, and pricing have, in fact,

1 resulted in the lowest storm recovery charge consistent
2 with market conditions at the time the storm recovery
3 bonds are priced and based on information available
4 through the date of pricing.

5 Furthermore, while the IAL provides some
6 assurance, the Commission should enhance the
7 protections needed to ensure a conflict-free process by
8 its involvement in the complete process in issuing
9 these bonds and requiring certificates from not only
10 the Companies, but also from the bookrunning
11 underwriters and the Public Staff's financial advisor.
12 My testimony delineates a number of personal
13 experiences where investment banker assurances were not
14 sufficient in protecting the transaction.

15 This concludes my summary.

16 Q. Thank you, Mr. Schoenblum.

17 MR. CREECH: Chair Mitchell, the witness
18 is available for cross examination; however, I
19 believe we have one final panelist.

20 MR. GRANTMYRE: This is Bill Grantmyre
21 again, Public Staff. Mr. Moore, are you online
22 now?

23 THE WITNESS: (William Moore) Yes, I
24 am.

1 CHAIR MITCHELL: Mr. Grantmyre, just
2 make sure your camera is on.

3 DIRECT EXAMINATION BY MR. GRANTMYRE:

4 Q. Mr. Moore, did you cause to be prefiled --
5 please state your name and address.

6 A. (William Moore) William Moore. 2764 North
7 North Shore Court, Wichita, Kansas.

8 Q. And by whom are you employed?

9 A. Well, I'm retired, but I'm acting as a
10 consultant for Saber Partners and the Public Staff.

11 Q. And did you cause to be prefiled on
12 December 21, 2020, direct testimony consisting of
13 16 pages and no exhibits?

14 A. Yes.

15 Q. And if I asked you those same questions
16 today, would your answers be the same?

17 A. Yes, they would.

18 Q. And you have no corrections to any of your
19 testimony; is that correct?

20 A. I do not.

21 MR. GRANTMYRE: Madam Chair, I would
22 request that his direct testimony be copied into
23 the record as if given orally.

24 CHAIR MITCHELL: All right.

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Mr. Grantmyre, the prefilled testimony of witness Moore consisting of 16 pages will be copied into the record as if given orally from the stand.

(Whereupon, the prefilled direct testimony of William Moore was copied into the record as if given orally from the stand.)

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

Docket No. E-2, Sub 1262

Docket No. E-7, Sub 1243

In the Matter of

Joint Petition of Duke Energy)
Carolinas, LLC and Duke Energy)
Progress, LLC Issuance of Storm)
Recovery Financing Orders)

DIRECT TESTIMONY OF
WILLIAM B. MOORE
CONSULTANT TO SABER
PARTNERS, LLC

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION**Docket No. E-2, Sub 1262****Docket No. E-7, Sub 1243****Direct Testimony of****William B. Moore****December 21, 2020****TESTIMONY OF WILLIAM B. MOORE****DECEMBER 21, 2020**

1 **Q. Please state your name and address.**

2 A. William B. Moore, 2764 North Northshore Court, Wichita, KS, 67205.

3 **Q. What is your relation to Saber Partners LLC?**

4 A. I am a Consultant to Saber Partners, LLC (Saber Partners or Saber).

5 **Q. Please describe your educational background and professional**
6 **experience.**

7 A. I have a Bachelor of Business Administration, Cum Laude
8 Concentration in Accounting, from Wichita State University. I also
9 was a student, then advisor and eventually faculty at The University
10 of Michigan Public Utility Executive Program.

11 I retired in 2011 as CEO and President of Westar Energy, then the
12 largest electric utility serving Kansas, and currently serve on the
13 Boards of Directors of several banking and civic organizations. For
14 over thirty-three years I held positions in general management,
15 operations, corporate finance, strategic planning, financial relations,
16 investor relations and financial reporting in the energy sector. I have

1 significant experience in arranging and closing numerous types of
2 financial transactions. For example, working at the executive level, I
3 directed and implemented with our teams, restructuring plans to
4 restore operational and financial health to Westar Energy (2002-
5 2011) and Kansas Gas and Electric Company (1987-1992). I also
6 have had executive involvement in establishing the strategic
7 direction for companies, including acquisitions, acquisition defense,
8 mergers and divestitures of significant business units.

9 More specifically, I served as President, Chief Executive Officer and
10 Board member at Westar from 2007 until 2011, following four years
11 in roles as Vice President, President and Chief Operating Officer,
12 with operating responsibility for Power Delivery, Customer Care,
13 Environmental and Safety.

14 Prior to my years at Westar, I served as the Senior Managing
15 Director for Saber Partners LLC, from 2000-2002. The firm was
16 formed to provide unique senior level corporate financial advice.
17 Clients included the Public Utility Commission of Texas on the
18 issuance of "transition bonds" (Ratepayer-Backed Bonds) resulting
19 from deregulation. At that time, we also provided a small mid-western
20 distribution utility general corporate advice regarding the company's
21 transition from a member-owned organization to a publicly-traded
22 utility. We also were retained by the State of California to provide
23 advice to the Governor regarding the State's energy crisis.

1 During the 1990's, I served in several roles at Western Resources,
2 Inc. (WR), Topeka, Kansas (1992-1995 as Vice President-Finance
3 and 1998-2000 as Executive Vice President and CFO). From 1995-
4 1998, I returned to Kansas Gas and Electric Company (KGE) in
5 Wichita, Kansas as Chairman and President.

6 At WR as the senior financial executive reporting to the CEO, I
7 implemented the financial strategy of the electric utility operations.
8 As CFO, I addressed analyst earnings projections that were
9 significantly too high and the refinancing plans for a major
10 diversification subsidiary. I negotiated over \$1.5 billion of bank
11 facilities for WR and its subsidiaries during a period of declining credit
12 quality and the restatement of financials. I also established a \$150
13 million facility to allow sale of accounts receivable, reducing interest
14 costs by \$1 million to \$2 million per year.

15 Earlier in my tenure at WR, I was instrumental in the analysis,
16 negotiation and sale of certain gas distribution properties (\$400
17 million), restructured the long-term debt portfolio and negotiated
18 terms and conditions for the issuance of over \$1.4 billion of debt and
19 equity.

20 A highlight of my time as Chairman of the Board and President of
21 Kansas Gas and Electric Company, a wholly owned subsidiary of
22 WR with \$650 million in revenues and 280,000 customers, was my
23 work enhancing financial performance and resolving conflict,

1 improving relationships with communities, key customers,
2 regulators, politicians and employees by increasing visibility of KGE
3 leadership which had been significantly reduced as a result of the
4 merger which formed WR.

5 My career at KGE, the stand-alone company, included two merger
6 attempts, both while I was CFO. In 1990, as one of the key
7 representatives for KGE, I managed the merger activities and
8 successful defense against the first hostile takeover attempt of a
9 major investor-owned electric utility: shareholder value was
10 enhanced by \$150 million. The second was the successful merger
11 which formed WR.

12 Over the course of my career at KGE, I negotiated terms and
13 conditions for the issuance of over \$3 billion of both investment grade
14 and non-investment grade securities. Issuances were required to
15 finance the fuel diversification program which resulted in the
16 construction of over 4600 MW of coal and nuclear generation, and
17 we accessed both European and domestic markets.

18 Through the years, I have been responsible for many facets of
19 corporate finance, cash management and investor relations, and
20 have been focused on using best practices for corporate financial
21 strategies, procedures, and standards. Here are two more examples
22 of refinancings that netted significant savings. I directed and
23 negotiated the refinancing of \$327 million of floating rate tax exempt

1 bonds at 7% for 40 years. Our decision to stay short– initially due to
2 low credit rating and high long-term rates– saved over \$100 million
3 in interest expense.

4 A second example is the negotiation of the sale/leaseback of a coal-
5 fired generating station in 1987, which we refinanced in 1992. We
6 recognized a \$300 million gain, and then efficiently used credits to
7 limit tax liability to \$50 million. We found one investor who took the
8 entire equity interest and were able to close without expensive bridge
9 financing.

10 I currently serve in several Board of Director positions, including
11 Fidelity Bank (Director and Audit Chair), Wichita State University
12 Foundation (Director, Past Chair and Governance Committee) and
13 Sedgwick County Zoo (Trustee and Finance Committee). I have
14 enjoyed similar roles at other great institutions including: Intrust
15 Financial Corp and Intrust Bank in Wichita Kansas; Wichita Area
16 Chamber of Commerce; United Way Campaign Chair, Goodwill
17 Industries, Kansas Big Brothers/Big Sisters and others.

18 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

19 A. To support the need for a Bond Team that includes active
20 Commission and Public Staff representation with its independent
21 advisor.

1 **Q. BASED ON YOUR PAST EXPERIENCE IN THE ELECTRIC**
2 **UTILITY INDUSTRY, DO YOU HAVE RECOMMENDATIONS**
3 **ABOUT WHAT THE COMMISSION SHOULD INCLUDE IN ITS**
4 **FINANCING ORDER IN THIS PROCEEDING?**

5 A. Yes. I have been in finance most of my career, I know how much
6 time and effort goes into a financing that is not what one would call
7 a “plain vanilla” bond. Many items and decisions are made as the
8 process goes forward. Few things can be decided up-front and
9 locked in. Document sessions, underwriter selection, rating agency
10 reviews, marketing, the pricing process and more are dynamic. All
11 decisions made during this time will affect the cost to the ratepayers
12 directly. The Ratepayer-Backed Bond process that I witnessed in
13 2001 in Texas and as described by the Companies and Public Staff
14 witnesses are clearly more complex than traditional utility first
15 mortgage bonds or unsecured debt. I believe the Commission’s
16 Financing Order needs to adapt to this situation.

17 **Q. HOW SHOULD THE COMMISSION ADAPT?**

18 A. The main proposal I have seen and support is for the Commission to
19 create a post financing order, but pre-bond issuance, review process
20 that includes a Bond Team. The Bond Team has the Companies and
21 its advisors, Public Staff and its advisors and the Commission staff
22 involved in all matters involving the structuring marketing and pricing
23 of the bonds. At the end of the process, when the bonds get priced,

1 each of the parties involved would give a certification that ratepayers
2 got the best deal possible at the time – the lowest storm recovery
3 charges consistent with market conditions and the terms of the
4 financing order.

5 **Q. WHY DO YOU SUPPORT THE BOND TEAM APPROACH?**

6 A. As a utility executive, I like the Bond Team approach. One of my main
7 reasons for this is because the certification being required is not only
8 from the Underwriters and Companies, but also from the ratepayer
9 advisors. This brings all the parties together.

10 Financial opinions are used extensively in many transactions like
11 mergers and acquisitions where we get “fairness opinions”. In those
12 transactions no one relies on a single opinion from one side of the
13 transaction. Each side seeks an independent view and opinion.

14 Because the Financing Order is irrevocable and the Commission is
15 required to give up its regular ongoing review of the costs, the Bond
16 Team approach, together with confirming certifications, and with the
17 additional layer of independent confirmation from the ratepayer
18 representatives, confirms that the lowest storm recovery charge was,
19 in fact, achieved. This would give me comfort that the Commission
20 was fully informed and satisfied with the results.

1 **Q. WHY IS THIS IMPORTANT?**

2 A. I believe all utilities understand the importance of keeping customers'
3 rates as low as possible while still delivering reliable energy and
4 excellent customer service. The fact that "AAA" rated storm recovery
5 bonds are being issued is a perfect example of a "win" for ratepayers
6 and also for the Companies. No matter what the "AAA" interest rate
7 will be, it will still be significantly less than the Companies' respective
8 weighted average cost of capital.

9 But that is not the requirement or the objective of this transaction –
10 just to produce savings compared to the utility's cost of capital. The
11 objective and requirement here is to achieve the "lowest" storm
12 recovery charge, of which interest rate is only one part. It does not
13 make sense to me that a party representing the utility, who is not
14 responsible for repaying the bonds, would be present but that no
15 party representing the ratepayer would be present "at the negotiating
16 table" throughout the many steps in structuring, marketing and
17 pricing these Ratepayer-Backed Bonds. Markets work best when
18 everybody who has a financial interest in the outcome has a say in
19 what happens. Here the ratepayer has the most at stake in the bond
20 offering, and the Companies are protected from any of the costs of
21 the deal. Representatives of the ratepayers should be involved and
22 should have an independent advisor to assist them in the process
23 because these things are very technical.

1 **Q. WHICH OF THESE STEPS DO YOU BELIEVE RECEIVE THE**
2 **MOST BENEFIT FROM HAVING AN INDEPENDENT ADVISOR**
3 **ON THE BOND TEAM?**

4 A. They all contribute to achieving the lowest storm recovery charge,
5 but in my experience, marketing and pricing are the most important
6 steps requiring proactive independent advisor involvement for the
7 ratepayer.

8 My perspective is that of a former treasurer and then chief financial
9 officer and finally CEO with the utility finance function reporting to
10 me. I have interacted with investment bankers and underwriters
11 directly for years. I agree completely with witnesses Schoenblum and
12 Maher that in all security issuances, underwriters have an inherent
13 conflict of interest in determining the appropriate pricing level of the
14 bonds. The testimony of witnesses Heath and Atkins seem to miss
15 this important point. This conflict of interest in a Ratepayer-Backed
16 Bond transaction is critical especially if the ratepayer is not at the
17 negotiating table. I have found that it is not wise to rely on
18 underwriters without a lot of work to keep the process competitive
19 and honest. Wall Street has its own goals that do not always align
20 with goals of the issuer. The process works best when you do your
21 own homework and not just defer to others.

1 **Q. WHY DO YOU SAY THAT?**

2 A. Regarding marketing, as witness Atkins testifies, extensive
3 education of investors will be provided by the underwriters working
4 with the Companies. But I've seen that underwriters don't always get
5 it right. The attention and focus varies greatly. That's why we liked
6 firms that had research departments and bankers who spent the time
7 to get to know us thoroughly and could explain things about our
8 company and credit clearly. Companies that come frequently to
9 market like Duke Energy benefit from a lot of attention and focus.
10 Duke is covered and studied and can access the market easily. But
11 this is not a Duke traditional bond. And there have been only three
12 other bonds like this that have been sold in the past 5 years. It
13 probably has not received a lot of attention from underwriters or
14 investors because there really has been no reason for them to focus.
15 Without a strong marketing plan focused on extensive education of
16 investors, this is going to be a problem with something that has been
17 around for a long time, but few know very well.

18 **Q. WHAT SHOULD THE COMMISSION CONSIDER TO ADDRESS**
19 **THIS ISSUE?**

20 A. The Commission and Public Staff with their advisors need to be
21 involved in that education process which is the important part of
22 marketing. Having direct input into what is being presented, how it is
23 being presented and to whom will make sure it is being done right for

1 the ratepayer. Direct involvement in the process helps ensure that
2 the underwriters actually stimulate broad investor demand as
3 opposed to distribute to a few large accounts. As a presenter of
4 information at many road shows and conference calls with investors,
5 it was always difficult to determine those with real interest in the
6 security. But by speaking and hearing from investors I got a better
7 sense of what needed to be done. I also learned that I should not just
8 speak with the investors one underwriter recommends but to listen
9 to many and try to get to smaller accounts.

10 **Q. WHY IS BROAD DISTRIBUTION TO SMALLER ACCOUNTS**
11 **IMPORTANT?**

12 A. Most underwriters know and cover the large institutions, like
13 Blackrock and Pimco and Nuveen. It's easy to sell to them because
14 their size gives them market power. They write big tickets which
15 means they buy large amounts. An underwriter can sell a lot of a
16 security with a single phone call. When there is a large order, that
17 investor usually gets more influence over the price or yield on the
18 bond because the underwriter can sell the deal quickly and move on
19 to the next deal. I found getting really broad distribution and
20 competition among investors takes more time and effort. So instead
21 of one call, they need to make 50 calls. And instead of one order for
22 \$50 million it is 10 orders for \$5 million. Some bankers are willing to
23 make the effort, others not so much. With the ratepayer

1 representative involved and taking the time to help educate investors
2 and get them interested, it is more likely to result in a broader
3 distribution with a positive outcome, lower cost.

4 **Q. HOW SHOULD THE ACTUAL PRICING BE VIEWED BY THE**
5 **COMMISSION?**

6 A. Witness Atkins stated “The underwriters, in conjunction with the
7 issuer, will begin to discuss informally with investors.....the credit
8 spread relative to the benchmark rates for each tranche”.

9 This is one of the most important parts of the process getting the right
10 benchmark and value assigned to bonds at each maturity. Witness
11 Sutherland has done the most work on the appropriate pricing levels
12 and comparables for this type of Ratepayer-Backed Bond. Witness
13 Maher who was at AAA-rated Exxon discussed how they would
14 approach the value of their securities versus what the bankers told
15 them. I agree that one has to have a view, a perspective on the value
16 of what you are selling from which to negotiate with underwriters and
17 investors. This part of the process needs the ratepayer advisor
18 perspective before those on the other side of the negotiating table
19 have informal investor discussions. They need to be involved in
20 determining the appropriate benchmarks, the initial thoughts on
21 tranches and what the credit spread range should be relative to
22 benchmark.

1 **Q. ARE NOT THOSE ITEMS ALREADY KNOWN LARGELY? THE**
2 **MARKET IS EFFICIENT WHEN YOU GET AAA RATING,**
3 **CORRECT?**

4 A. I said earlier that the AAA rate would be below the Companies' cost
5 of capital, but there is no single AAA-rate out there in the market.
6 Valuations vary greatly in all rating categories. This is a process that
7 requires effort. The work of witness Sutherland on appropriate
8 benchmarking impressed me. The results that Saber Partners have
9 achieved in each of their 13 transactions speaks for itself.

10 **Q. WHAT WOULD THAT INVOLVEMENT LOOK LIKE?**

11 A. The Bond Team and especially Public Staff's advisors should be a
12 party to all meetings and on all telephone calls to present their views
13 and receive the feedback firsthand and in real time. This step is key
14 because it is the beginning of the underwriters, as witness Atkins
15 states, "keeping the master record (known as 'the book') in which all
16 indications of interest received by underwriters from potential
17 investors are recorded".

18 It is important for the Commission and Public Staff to have full
19 transparency of "the book" to ensure that underwriters have reached
20 out to a wide range of investors. That starts with the informal investor
21 discussions and carries through Launch, Allocation and Pricing.

1 This it is not just listening and accepting what the underwriters report
2 in what witness Atkins calls their “professional judgment.” It requires
3 due diligence both through communication with underwriters in the
4 deal as well as those outside of the immediate process.

5 As discussed in my professional experience, I have been involved in
6 raising over \$4 billion in issuance of bonds and equity. Ability to have
7 full transparency of “the book” was always a challenge. In my case,
8 underwriters would typically provide a percentage of under- or over-
9 subscribed (amount of orders versus shares or bonds offered for
10 sale), but were very protective of how many investors had indicated
11 interest and their levels, price and amount. Without that information
12 we had no idea of how hard the salesforce was pushing our
13 securities and overall demand. Our relationship managers/calling
14 officer would sometimes be willing to provide more information, but
15 it always seemed to put them at risk to share that information, if they
16 knew it. Reaching out to potential investors we knew could also help
17 us verify (or not) what the underwriters were providing. More than
18 once did we find out after pricing that “the book” was 150 to 200
19 percent over-subscribed, which meant we left some basis points on
20 the table.

21 The Commission, Staff and Public Staff should not want that to
22 happen on this issue of storm recovery bonds. By following “best
23 practices” as outlined in the testimony of witnesses Schoenblum and

1 Fichera, the Commission will have all the steps in place to achieve
2 the lowest storm recovery charge benchmark.

3 **Q. DOES THE FACT THAT THE PUBLIC STAFF IS AN INTERVENOR**
4 **IN THE COMPANIES' GENERAL RATE CASES AFFECT YOUR**
5 **OPINION ABOUT WHETHER THEY SHOULD BE ON THE BOND**
6 **TEAM?**

7 A. No.

8 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

9 A. Yes.

1 Q. Do you have a summary of your testimony?

2 A. Yes, I do.

3 Q. Would you please read your testimony?

4 A. I will. Good morning, Commissioners. The
5 following is a summary of my testimony.

6 I retired in 2011 as president and CEO of
7 Westar Energy after a 33-year career in the electric
8 utility industry. Most of my career was in the
9 financial area as finance assistant, treasurer, VP
10 finance, EVP finance, and CFO. During those years, I
11 negotiated terms and conditions for the issuance of
12 over \$3 billion of both investment-grade and
13 non-investment-grade securities, \$1.5 billion of bank
14 facilities, over \$1 billion of equity, and several
15 other ways of sourcing funds such as a power plant
16 sale/leaseback, sale of accounts receivable, and
17 floating rate pollution control bonds. My investor
18 relations responsibilities included many meetings with
19 analysts and investors to provide information on our
20 company and to hopefully raise interest in our
21 securities.

22 The purpose of my testimony, as a former
23 utility CEO and CFO, I support the need for a bond
24 team. It is the right thing to do for ratepayers. It

1 is also common sense given the unique nature of these
2 Ratepayer-Backed Bonds. The bond team should include
3 active Commission, Staff, and Public Staff
4 representation with its independent advisor in all
5 aspects of structuring, marketing, and pricing the
6 proposed storm recovery bonds.

7 Most importantly, the structuring, marketing,
8 and pricing of Ratepayer-Backed Bonds are more complex
9 than that of plain vanilla utility bonds, such as first
10 mortgage bonds. This is because ratepayers are
11 directly responsible to repay the bonds and associated
12 financing cost through a nonbypassable, automatically
13 adjustable rate component. In this case, storm
14 recovery charge with the Commission required to give up
15 future review.

16 It is a good business practice and common
17 sense that the party directly responsible for repaying
18 the bonds, and that's the ratepayer, should be at the
19 negotiating table throughout the many steps in
20 structuring, marketing, and pricing the
21 Ratepayer-Backed Bonds. Everything that occurs in the
22 structuring and marketing of the bonds leads into the
23 most important part, the bottom line of this
24 transaction, pricing.

1 My 33-year experience with Wall Street on
2 many securities offerings has shown me it is not always
3 wise to rely solely on the underwriters' professional
4 judgment when pricing bonds. Wall Street wants all
5 sales force and investor inputs funneled through the
6 bookrunning manager/underwriters. Westar had an
7 investor relations team that often talked to owners of
8 our securities directly before and after securities
9 offerings. For Ratepayer-Backed Bonds, ratepayer
10 representatives should have eyes and ears on what the
11 underwriters are saying to and hearing from potential
12 investors before floating price talk.

13 Because the financing order is irrevocable,
14 the Commission must give up its regular ongoing review
15 of these costs. The bond team approach would provide
16 independent confirmation that the lowest storm recovery
17 charge, in fact, was achieved. A bond team that
18 includes Commission, staff, and Public Staff
19 representatives should have the mandate to be involved
20 in first-hand discussions with the sales force and
21 investors to be effective in helping to achieve the
22 lowest storm recovery charge benchmark.

23 This completes my summary.

24 MR. GRANTMYRE: The witness and the

1 panel are available for cross examination.

2 CHAIR MITCHELL: All right. Duke, you
3 may proceed.

4 MR. JEFFRIES: Thank you,
5 Chair Mitchell. This panel will have two lawyers
6 asking questions, and I will be cross examining
7 Mr. Moore, and Mr. Maher, and Mr. Fichera; and
8 Ms. Athens will be addressing her questions to
9 Mr. Schoenblum. And I think the order that we
10 intend to ask our questions is that I will question
11 Mr. Moore first, then Mr. Maher. Ms. Athens will
12 question Mr. Schoenblum, and we'll finish up with
13 Mr. Fichera, if that's all right with the
14 Commission.

15 CHAIR MITCHELL: You may proceed.

16 MR. JEFFRIES: Thank you.

17 CROSS EXAMINATION BY MR. JEFFRIES:

18 Q. Mr. Moore, I've got some questions for you,
19 sir.

20 In your testimony, you indicate you have
21 significant experience placing corporate debt under the
22 capital markets; is that right?

23 A. (William Moore) Yes.

24 Q. And as you mentioned, that experience was

1 gained in the context of your work for Westar Energy
2 and Kansas Gas & Electric, right? I'm sorry, did you
3 say yes?

4 A. Yes.

5 Q. Okay. Thank you. Would you agree with me
6 that the process used to market, price, and sell
7 long-term corporate bonds is a well developed one?

8 A. I would agree that.

9 Q. And the principal parties that are typically
10 involved in issuance of long-term corporate bonds are
11 the issuer, the underwriters, and there's often more
12 than one underwriter, and the investors, correct?

13 A. That is correct.

14 Q. All right. And, of course, the issuers and
15 the underwriters all have their own counsel as well; is
16 that correct?

17 A. Yes, they do.

18 Q. Okay. And while the details of each deal and
19 how negotiations proceed may be different, the basic
20 process is that -- that has developed in the capital
21 markets is largely the same, correct?

22 A. It was during my time.

23 Q. Okay. Fair enough. I'd like to talk to you
24 about due diligence a little bit. In your testimony,

1 you indicate a belief that it's necessary for the
2 Public Staff to conduct due diligence on the bond
3 marketing pricing and issuance process, correct?

4 A. Yes, I did.

5 Q. And by due diligence, you mean confirming
6 that what the underwriters' issuers and issuer advisors
7 tell the Public Staff about discussions or negotiations
8 with potential investors and their representatives is
9 true; is that what you mean by that?

10 A. I agree with that, as far as what they are
11 going to tell them, but also I'm talking about what
12 they heard back from those investors and other people.

13 Q. Right. Which obviously necessitates them to
14 communicate with them directly, correct?

15 A. Are you referring to the underwriter --

16 Q. To --

17 A. -- or Company?

18 Q. The conversation between the Public Staff or
19 the Public Staff representatives and the parties from
20 whom you are seeking confirmation of information that
21 requires them to communicate with each other in order
22 to provide that confirmation that you're discussing,
23 that due diligence.

24 A. Were you talking about the Public Staff?

1 Q. Yes.

2 A. Are you talking --

3 Q. Yes.

4 A. Yes, it would require discussions with -- to
5 get the due diligence, I think what we are talking
6 about here is that process being done through their
7 advisor.

8 Q. Okay. And you also mentioned that it would
9 be important to communicate -- and again, this is on
10 page 16 of your testimony, but it would be important to
11 communicate with those outside of the immediate
12 process; do you recall that statement?

13 A. Excuse me, I'll open my -- I'll open my
14 testimony.

15 Q. Sure.

16 A. Could you point me to the page again?

17 Q. Yeah, hold on. I should have had it opened
18 already, but I need my copy. No. Public Staff
19 testimony. Okay. There we go. Sorry for the delay
20 here.

21 (Pause.)

22 Q. Well, I may have that wrong. So let's go on
23 to the next question. I apologize for that.

24 Would these -- would these conversations, the

1 conversations in the conduct of due diligence that you
2 might engage in on behalf of the Public Staff, would
3 that -- would that include communications with
4 potential investor representatives?

5 A. Yes.

6 Q. Okay. And potentially with the investors,
7 themselves?

8 A. Yes. We'd like to be getting market
9 intelligence as to what they're thinking, what they're
10 hearing, and would like it to be direct.

11 Q. Sure. And I'm just trying to determine what
12 the universe is of folks that you believe it would be
13 appropriate to communicate with. So would it also
14 include rating agencies?

15 A. If it was necessary, as part of the bond
16 team, and that there's questions coming back from the
17 rating agencies regarding the documentation presented
18 to the rating agencies.

19 Q. And would you might also have discussions
20 with the SEC?

21 A. Again, in response to questions that they
22 might ask, and they might reach out directly to us.

23 Q. Mr. Moore, when you were managing debt
24 issuances for Westar, did you ever allow a third party

1 to conduct this type of due diligence with respect to a
2 security you were issuing?

3 A. We did not -- we never had anyone ask to
4 participate.

5 Q. Okay. Thank you. In your testimony, you
6 discuss the importance of certification, that the
7 statutory cost objectives have been achieved by the
8 participants in the securitization bond issuance; is
9 that correct?

10 A. Yes, I do.

11 Q. Okay. And is it your understanding that DEC
12 and DEP intend to certify to the Commission that the
13 issuance of bonds in this proceeding is consistent with
14 the statutory cost objectives?

15 A. I'm not sure how to answer that. I know
16 they've talked about the issuance advice letter, and
17 I'm not fully remembering, maybe, what they were saying
18 they would say under that kind of a certification.

19 A. (Joseph Fichera) Perhaps I could add to
20 Mr. Moore, that the -- it's consistent with both the
21 statute and the financing order, would be the standard.
22 And I think that's what we're all talking about now is
23 what should be in the financing order, as there was a
24 decision yesterday about the additional conditions

1 based on the -- I guess it's called the catch-all thing
2 that the legislature gave the Commission to add any
3 conditions that it wanted in order to protect
4 ratepayers or whomever, that were not inconsistent.
5 And that is what was done in Florida, as well. A
6 phrase similar to that was in the Florida storm
7 securitization, and that's how the Florida Commission
8 established the lowest cost, standard, as well as bond
9 team and various other things. So I think that's --
10 for the edification of the Commission, that's what
11 we're talking about right here, what would be the
12 certification that would be involved.

13 MR. JEFFRIES: Chair Mitchell, I think I
14 may need some help from the Commission here. One
15 of the benefits of presenting witnesses in panel
16 format is the ability, particularly on direct and
17 redirect, for the witnesses to comment on each
18 other's testimony or help answer questions. We
19 have -- on cross, however, it's a little more
20 problematic, because we have two lawyers that are
21 attempting to cross examine these witnesses on
22 their testimony, and our questions, Ms. Athens'
23 questions and my questions, are all directed toward
24 specific witnesses based on their testimony.

1 And what Mr. Fichera just did is in some
2 ways fine, but it's also very problematic for us to
3 be able to effect -- to engage in effective cross
4 examination because, to the extent, particularly if
5 it's -- if I'm questioning one witness and another
6 witness who handled by Ms. Athens shows up, then
7 she's either forced to cross in the middle of my
8 cross or I'm forced to cross a witness that I
9 haven't prepared for.

10 So I think it's fine for Mr. Creech and
11 Mr. Grantmyre to ask follow-up questions on
12 redirect, that's obviously their right, but I would
13 ask for some help, if we could, to have the
14 questions that I ask answered by the witnesses that
15 they are directed to.

16 THE WITNESS: I'm sorry, we were advised
17 that we were able to do that. But whatever the
18 Commission says, I'm sorry if I interrupted. But I
19 was advised that that was what we -- when bringing
20 a panel, that since we were a team, we would be
21 able to supplement things rather than just
22 simply -- but whatever the Commission would --

23 CHAIR MITCHELL: Mr. Grantmyre, would
24 you like to be heard?

1 MR. GRANTMYRE: Yes. I think it's
2 normal practice before the Commission, when we have
3 a panel, if another panelist has very pertinent
4 follow-up information, that they be permitted to
5 give it, and we would ask that this practice
6 continue. I do point out that Mr. Fichera is also
7 a witness that Mr. Jeffries will cross examine, as
8 is Mr. Maher, and Ms. Athens only has
9 Mr. Schoenblum. But we feel that, on a panel, it
10 is very important if the witness -- another witness
11 has pertinent information that gives information to
12 the Commission, that they be allowed to supplement
13 answers.

14 CHAIR MITCHELL: All right. Thank you,
15 Mr. Grantmyre. Mr. Jeffries, you know, allowing
16 witnesses to testify or having witnesses testify
17 before the Commission in a panel is something that
18 typically occurs around here. It's my
19 understanding and experience that the parties agree
20 to that beforehand, and so, you know, if a member
21 of the panel has a response -- let me be clear. So
22 that when questions are asked, they're asked of the
23 panel, not of a particular witness.

24 We are sometimes more relaxed in our

1 enforcement of the panel procedures than in other
2 cases. So I understand the practical difficulties
3 that having a panel of witnesses poses to the cross
4 examiner. I'll just say do your best to get
5 through this, and I will advise other counsel the
6 same. We'll give you the time you need to get
7 through your cross examination.

8 And with that, we are at our morning
9 break. We will go off the record now. We will
10 resume at 11:00. We are off, and we'll be back at
11 11:00. Thank you very much.

12 (At this time, a recess was taken from
13 10:47 a.m. to 11:00 a.m.)

14 CHAIR MITCHELL: Before we begin, we
15 will break for lunch at 12:30. All right.

16 Mr. Jeffries, you may proceed.

17 MR. JEFFRIES: Chair Mitchell, the
18 Company appreciates your ruling before the break,
19 and I do have one slight indulgence I would request
20 with regard to that ruling, and that is, in order
21 for the Company to establish a reasonable record on
22 cross, I would simply ask that the witness to whom
23 my question or Ms. Athens' question is originally
24 directed, if they could provide their answer before

1 additional answers are provided by the other
2 witnesses. If that's not going to inconvenience
3 anyone, that would help us a lot in keeping the
4 structure of our cross examination outlines.

5 CHAIR MITCHELL: Mr. Grantmyre?

6 MR. GRANTMYRE: The Public Staff does
7 not oppose that.

8 CHAIR MITCHELL: Okay. All right. We
9 will proceed as such. Gentlemen, I believe you've
10 heard Mr. Jeffries' request that you-all do your
11 best to answer the questions that are directed to
12 you before other members of the panel respond.

13 All right. Mr. Jeffries, you may
14 proceed.

15 MR. JEFFRIES: Thank you,
16 Chair Mitchell.

17 Q. Mr. Moore, just a couple more questions for
18 you. I take it that you are familiar with the -- what
19 the Company refers to as the statutory cost objectives
20 that are set forth in G.S. 62-172; is that right?

21 A. (William Moore) Somewhat. I mean, I have
22 read them and tried to interpret them, but the lowest
23 cost storm reserve charge, so lowest storm reserve
24 charge.

1 Q. Okay. Yeah, that's right. And I'll accept
2 that as a paraphrasing of the statutory language, how
3 about that?

4 Were you -- were you listening to the hearing
5 yesterday when Mr. Heath testified?

6 A. Yes, I was.

7 Q. Okay. And then you heard him testify
8 yesterday, and it's also in his rebuttal where he
9 indicates the Company will not only comply with that
10 requirement but will also provide a certificate to the
11 Commission regarding that requirement, correct?

12 A. I believe I heard that. I thought I heard
13 some different conversation on that, but it sounded to
14 me like they were the only one going to give a
15 certification, not the underwriters, not us, not Saber
16 Partners, put it that way. So that's what I thought I
17 heard.

18 Q. All right. Thank you. You don't have any
19 reason to believe that Mr. Heath was being untruthful
20 about his intent to comply with the statutory standard
21 or provide a certification to that effect to the
22 Commission, do you?

23 A. I do not.

24 MR. JEFFRIES: That's all the questions

1 I have for Mr. Moore.

2 MR. GRANTMYRE: The Public Staff would
3 do redirect after all the -- or would the Chair
4 prefer that we do redirect now? I would do it
5 after all the panels have gone.

6 CHAIR MITCHELL: Typically -- I
7 apologize for interrupting you, Mr. Grantmyre.
8 Typically, cross examination occurs of the panel,
9 and then we'll move to redirect for the panel. So,
10 Mr. Jeffries, let's proceed as such.

11 MR. GRANTMYRE: Thank you.

12 MR. JEFFRIES: Thank you,
13 Chair Mitchell. The next set of questions I have
14 are for Mr. Maher.

15 Q. Mr. Maher, you have quite a bit of experience
16 in issuance of corporate bonds and the capital markets
17 from your time with ExxonMobil, correct?

18 A. (Brian Maher) That is correct.

19 Q. All right. You gave testimony, and on
20 page 5, you state that, as an officer of ExxonMobil,
21 you always expected to --

22 MR. JEFFRIES: I think I'm getting some
23 feedback. Is everybody else hearing that?

24 MR. CREECH: Mr. Maher, if you will

1 please mute -- well, he's muted now. Okay.

2 MR. JEFFRIES: All right. Let me try it
3 again.

4 CHAIR MITCHELL: All right.

5 Mr. Jeffries, just one minute, please, sir.

6 Mr. Maher, we're getting feedback from your line,
7 so we're going to mute you when you are not
8 speaking, all right? So when you speak, you're
9 going to need to take yourself off mute.

10 Mr. Jeffries, you may proceed.

11 MR. JEFFRIES: Thank you,
12 Chair Mitchell.

13 Q. Mr. Maher, in your testimony, you state that,
14 as an officer of ExxonMobil, you will also expected to
15 develop a cooperative and collegial relationship with
16 the banks that underwrote the bonds to achieve the
17 lowest overall cost possible for the financing; does
18 that sound familiar to you?

19 A. Yes. Yes.

20 Q. And that would be -- that would be the goal
21 of ExxonMobil when it issued corporate bonds, correct,
22 to achieve the lowest overall cost?

23 A. Yes, it would.

24 Q. Okay. And you don't doubt that this is also

1 the goal of Duke Energy when it issues long-term
2 corporate bonds, do you?

3 A. Well -- hold on. No. When they issue
4 long-term corporate bonds for themselves, yes, I agree
5 with that.

6 Q. Okay. When ExxonMobil -- when you were
7 issuing long-term debt instruments for ExxonMobil, I
8 assume that you communicated your desire to obtain the
9 lowest cost to your underwriters; is that correct?

10 A. Explain that, if I may. While we were doing
11 direct issues for ExxonMobil under my tenure,
12 particularly in the 1987 to '94 time, all of our issues
13 were done on a -- for standard debt on what we call the
14 negotiated competitive basis. So what that means is
15 that we would have a very collegial representative with
16 all the banks, because there were probably 25 of them
17 that would come in to see us, and we would be watching
18 what they were doing and what underwritings they were
19 doing. And we would pick probably the 10 that were
20 doing the best at the time, and we would talk to them
21 about an issue that we wanted to do.

22 And they would all give us preliminary ideas
23 of where we would price, probably in that range of 35,
24 40 basis points over U.S. treasuries. And we would

1 talk to them, and then what we would do is we would
2 pick 5 out of the 10 who we thought were doing the best
3 job at that time, and we would say -- let's say this
4 was Monday, we would say on Wednesday 9:00 there's
5 going to be a competition among you 5 and you will have
6 15 minutes to price, and whoever gets the best price --
7 gives us the best price we will take out of the 5 of
8 you.

9 So yes, it was collegiate, but we would take
10 the best out of the five. And as an example, what used
11 to be quotes of 35 to 40 basis points turned out to be
12 a final pricing of 10 to -- of 25 to -- 10 to 25 and
13 sometimes even 15 basis points. So what that proved to
14 us is that even though we were collegial and we were
15 friends, when we put the pressure on them, then they
16 would come down significantly in their pricing.

17 So that's the -- that's the conflict there.
18 And I guess I would have to also -- if I could take a
19 second, I talk about being aggressive, and I listened
20 to Mr. Heath's testimony and he talks about clearly the
21 statute talks about consistent with market conditions
22 at the time the bonds are priced. Well, you know, I
23 have a lot of respect for him and I have a lot of
24 respect for Duke, but I don't define market conditions

1 the same way that he does.

2 Underwriters, in my view, are part of the
3 market, as exemplified by how I just described we used
4 to issue the bonds. So, for me -- and this goes back
5 to that interesting conversation between Mr. Creech and
6 Mr. Heath, and the Commissioners got involved as well,
7 as to whether underwriters would be expected to own
8 parts of the bonds. Now, typically -- typically not,
9 but when they bid, I can tell you the winner would
10 probably more often than not wind up holding some of
11 those bonds, because they would bid at such a tight
12 price that they would own some until they could sell
13 them. They would hedge them against the Treasury so
14 they didn't lose large amounts or gain large amounts.

15 But the point is that my idea of an
16 aggressive marketing is not to wait until the
17 underwriter has all the investors ready and then say,
18 okay, that's the best we could do. In my -- in the
19 95/5 example that Mr. Creech gave, if we got there, we
20 would say to the underwriter -- if we were doing it, if
21 it were this kind of a deal, we would say, "Okay, it's
22 time for you to step up. You're making \$4- or
23 \$5 million on this deal, and it's time to step up and
24 take the last 5, because we don't want to pay more for

1 the other 95.

2 It's a difference in approach as to how you
3 define what market conditions you are and how
4 aggressive you are going to be with underwriters. And
5 we did do that on a couple of occasions where we had
6 more specialized transactions which involved
7 negotiating -- actual negotiated deals.

8 Q. So I think you may have answered a couple of
9 questions that I didn't ask, but that's fine. But to
10 return to the question I was getting to, the process
11 you described that you used with underwriters at
12 ExxonMobil, I mean, the entire purpose of that was to
13 minimize the cost to ExxonMobil of that debt, correct?

14 A. Correct.

15 Q. And I guess my point is that's the game,
16 right? I mean, that's the game the underwriters, and
17 issuers, and on the other side investors play. There's
18 nothing unique or secret about that, that that's what
19 these markets do. That's the purpose of this process,
20 correct?

21 A. It's the purpose, but the underwriters also
22 have investor clients in their trading desks, and what
23 they tell you is the lowest price most likely is not.

24 Q. And that's just the negotiating process. You

1 used a good technique to get a good result?

2 A. Right. And -- correct. And in this kind of
3 a transaction, we don't have them actually bidding for
4 all the bonds, but we would be there when the pricing
5 is taking place, and we would be making sure how we got
6 down to the absolute minimum price, even involving
7 underwriter ownership of some of the bonds before we
8 would say and now we got the lowest price.

9 Q. All right. Thank you. I'd like to talk a
10 little bit about the duties and interests.

11 A. (Joseph Fichera) Might I add one thing to
12 that? Having been at Bear Stearns and been one of
13 the -- in one of the banks that competed in that
14 process with Exxon, Exxon was a well-known credit and a
15 well-known company. And Brian's description about
16 being able to finance on Monday and do something on
17 Wednesday was able because they were well-known credit.

18 Here, in this situation, it's gonna be akin
19 to an initial public offering. This credit for DEC and
20 DEP established for the first time. Now, the
21 structure, as we said, has been known generally over
22 the past 20 years with \$50 billion issued. But when
23 you look at it, there's only about \$4 billion in this
24 huge capital market that's still outstanding. There's

1 only been a few issues. So the marketing period that
2 Brian did with Exxon and the competition was because
3 they were already an established credit.

4 Here, it's gonna probably be a little more.
5 I think Mr. Heath would agree with this. We have to
6 establish the credit, establish this and distinguish
7 this from others' credits and try to get the AAA that
8 it's not an asset, but it's actually a more corporate
9 security. I was glad to hear Mr. Heath say that
10 yesterday. That was something that they didn't start
11 out with in Florida saying, but we ultimately got there
12 through our testimony in Florida and through the bond
13 team in Florida.

14 So just got to distinguish, short marketing
15 periods for established credits are easy. This will be
16 a new credit, new issue, probably take a little more
17 time, but the same sort of competitive nature that
18 Brian is talking about wanting to create is what we
19 think the cooperative and collaborative efforts of an
20 established bond team working under a set of rules and
21 communication, how would we talk to the SEC, how we
22 would talk to rating, but be done.

23 Q. Mr. Maher, when you were -- when you were
24 involved in this process with underwriters in a

1 competitive process to try to get the best deal for
2 issuances of ExxonMobil bonds, those underwriters had
3 the same self-interest in those transactions as you've
4 described generally, correct?

5 A. (Brian Maher) Correct.

6 Q. Okay. And you certainly understood that they
7 had that self-interest at the time you went through
8 this process, correct?

9 A. Yes. And that's why we made them bid against
10 each other, because they all knew that each other had
11 the same self-interest.

12 Q. So you would agree with me, would you not,
13 that at least in your -- in the scenarios you're
14 describing, that the fact that they were
15 self-interested, that didn't prevent you from obtaining
16 what you believed to be the lowest price for the bonds
17 you issued, did it?

18 A. It didn't prevent me because -- yes, I would
19 agree. And it didn't prevent me because, when you have
20 five of the top banks bidding against each other, then
21 their self-interest to get the deal drives you to the
22 lowest transaction. It wasn't because they wanted to
23 get there.

24 Q. Well, of course not. I think we all

1 understand that. In your testimony, you spend some
2 time talking about this concept of fiduciary duty,
3 particularly within the debt issuance markets,
4 particular with respect to the proposed transaction,
5 and you mention some of that in your summary, the fact
6 that it's pretty commonplace to include waivers or
7 disclaimers of fiduciary duty and the documents -- the
8 relationship documents between underwriters and issuers
9 and that sort of thing.

10 I mean, this is -- this is not something new,
11 right, in the debt markets?

12 A. This is not something new in the debt
13 markets, but it's important to know it when the
14 underwriters are giving you their professional opinion
15 about what you should do.

16 Q. Sure. In fact, this whole dynamic where
17 underwriters and, I guess, potentially transactional
18 advisors disclaim fiduciary duty, that came out of a
19 lawsuit that was filed in -- back in 2005, right? You
20 said that in your testimony.

21 A. Yes. It certainly did indirectly. But
22 Goldman Sachs apparently did not have the fiduciary
23 responsibility -- didn't exercise the responsibility
24 that they should have to the IPL issuing company, and

1 eventually they were called on the carpet for not
2 exercising that responsibility, yes.

3 Q. So --

4 A. And then Hunt and Williams sent out a letter
5 to everybody saying based on that, we advise that all
6 underwriters should from now on include in their
7 underwriting contracts, a disclaimer of financial -- of
8 fiduciary responsibility, and they all did and have
9 done ever since.

10 Q. Yes. Us lawyers are bad about that. But the
11 fact that there's not a fiduciary duty between
12 underwriters or financial advisors and issuers, I mean,
13 that doesn't preclude those people from doing their
14 duty in an appropriate way, does it?

15 A. No. You know, I think -- I tried to give
16 that flavor of this in the transaction. Maybe it
17 sounds kind of strong, depending on who's reading it in
18 the other direction, but I think underwriters, they all
19 want to be perceived as doing good transactions.
20 Everybody -- Companies -- I'm sure Duke wants to be
21 perceived as doing a good transaction. The real
22 question is when it comes down to the actual
23 negotiating and how hard you negotiate, there can be a
24 lot left on the table because they don't have the same

1 incentives that we would and this Commission would to
2 protect the ratepayer.

3 Yes. My answer to your question is yes, they
4 do good transactions, but maybe not good enough or as
5 good as they could be.

6 Q. And your own example is an illustration of
7 the fact that, you know, despite the fact that
8 underwriters might have their own self-interest in
9 these transactions and despite the fact that there's no
10 fiduciary duty, you were able to obtain a result in
11 your finances that you felt represented the lowest
12 price. So, I mean, clearly those factors don't prevent
13 deals from being done appropriately, right?

14 A. As I said, I think very clearly throughout my
15 testimony, they -- it does not prevent deals from being
16 done appropriately as long as the issuer works very
17 hard to make sure that it happens.

18 Q. Sure. Mr. Maher, am I correct in thinking
19 you're not a lawyer, right?

20 A. You are correct.

21 Q. Okay.

22 A. I'm sure you figured that out by now.

23 Q. Well, I'm actually kind of curious in the
24 next couple of questions here. So you spend a

1 significant portion of your testimony talking about
2 fiduciary relationships, and then on page 12 of your
3 testimony, at least as I read it, and this is lines 3
4 through 6, you also say that you're not giving an
5 opinion as to whether a fiduciary obligation exists
6 between any parties to the proposed bond transactions;
7 did I get that right?

8 A. Right. I was quoting some things that were
9 quoted by witnesses, but I am not in a position myself,
10 not being a lawyer, to give opinion, correct.

11 Q. Well, so let me ask you this, then, because
12 as I read your testimony, about five pages later, on
13 page 17, at lines 8 through 12, you do make the
14 statement that Saber Partners has a fiduciary duty to
15 North Carolina customers, or at least they consider
16 themselves to have such a duty. So I was trying to
17 reconcile those two statements, and having some trouble
18 doing that.

19 A. Could you explain to me a little more about
20 why you think you were having trouble doing that?

21 Q. Well, I think we've established you're not a
22 lawyer, we've established that you testified that
23 you're testifying to who has a fiduciary obligation
24 with respect to the proposed bond transactions, but

1 then on page 17 you turn around and say that Saber has
2 a fiduciary duty to North Carolina customers. And I
3 guess I'm -- to me, those statements seem inconsistent.

4 A. Well, I say they consider themselves as
5 having it, right? And I guess there's -- and so that,
6 again, is not a definitive thing. But I will tell you
7 that there are other words that they have used which
8 are not in here because their contract with the
9 public -- with the Company -- I'm sorry, yeah, with the
10 Commission, Public Staff, you know, is not made public.
11 So I wasn't gonna go read through -- read all the
12 stuff.

13 But I can give you an example of some of the
14 words that are in there, because I've checked with
15 Mr. Fichera, and he said that it's okay to do that. He
16 said both Saber Partners, LLC and all the individuals
17 associated with Saber Partners, LLC are free from any
18 conflicts of interest and will provide the Public Staff
19 and the Commission with independent advice with an
20 exclusive duty of loyalty to the Public Staff and the
21 Commission.

22 So that, for me, sounds very much like what I
23 saw in all the other things that I used -- and I quoted
24 and used in my examples. And therefore, I was able to

1 make the conclusion that I believe that Saber has that
2 responsibility.

3 Q. Okay. Thank you for that.

4 A. (Joseph Fichera) And as representing Saber,
5 as Mr. Maher said, we're advisors, we're not
6 underwriters. We don't have a financial interest. We
7 give advice. And as you as a lawyer, I don't know what
8 your contract says, but I think there is considered a
9 duty of loyalty and a duty of care to the people, and
10 he put the interest of our clients above -- excuse me,
11 above any of our personal interests. And that's what
12 we think a fiduciary duty is.

13 I mean, I think you see a lot of commercials
14 on television these days where some of the brokers, or
15 Fisher Investments says, you know, aren't you getting
16 high fees. And they say, you know, we do better when
17 our clients do better because we're fiduciaries. And
18 that's sort of what we're saying here, that we're not
19 managing money. But we're giving advice that is in the
20 best interest. And we don't have any interest in the
21 bonds, but we're not trading them, we're not buying
22 them, we don't have interest in Duke stock.

23 And so our duty of care and our duty of
24 loyalty is to our client. Our client's objective is

1 the ratepayers, and so what -- we feel our duty flows
2 through to the ratepayer. It's just as simple as that.
3 You know, without getting a lot of lawyers involved, I
4 just think that's the common sense of contracts.

5 Q. So, Mr. Fichera, let me follow up on that
6 real quickly with you if that's all right.

7 A. Of course.

8 Q. Underwriters -- underwriters have an interest
9 in these transactions because they get paid for the
10 services they provide in conjunction with these
11 transactions, correct?

12 A. Not just that, they have lots of other
13 interests. I mean, they sell and trade them, they got
14 client relationships. I don't think it's just the fee.
15 It's not the -- it's not a fee for service.
16 Underwriting is not a fee for service like you or I are
17 being paid. Underwriting is something totally
18 different.

19 Q. So is your testimony that the fees that the
20 underwriters generate in these types of long-term bond
21 transactions are not an important aspect of the
22 benefits the underwriters get from these transactions?

23 A. They're one -- they're one benefit. They get
24 other benefits, but satisfying their customers' needs.

1 You know, I was an underwriter and, you know, we
2 really -- I was in corporate finance, not in sales and
3 trading. And look, you're balancing conflicts of
4 interest. You know, you got your sales and trading
5 department. I think I discussed this in my testimony.
6 They're interested, you know, in making money that way.
7 I in corporate finance, I had the relationships with
8 the companies. I want to make them happy, but I'm in a
9 separate P&L from my sales and trading force, different
10 interests are involved -- evolved.

11 I -- you know, in pushing -- when I went to
12 the -- went to my desk with Exxon -- saying Exxon's got
13 an opportunity, I think we should be -- have this
14 really a low spread to win this deal, I got pushed back
15 by traders saying that's crazy, we're not gonna do
16 that. And I, at one time, had a conversation when my
17 boss said to me, you know, you sound like them, Exxon.
18 And I said, well, when I'm talking to Exxon, I'm
19 representing you, but when I'm talking to you, I'm
20 representing them, because we're trying to bring people
21 together here.

22 So the sales and trading department and
23 underwriters, separate, lots of different
24 relationships, lots of things going on. And if you

1 ever notice, the underwriting isn't -- is not
2 considered a contract in the kinds of contracts you and
3 I have with our clients. There's no service that
4 simply says we're gonna buy these bonds at this price,
5 no representations. And as a matter of fact, the
6 underwriting agreement has Duke indemnifying or
7 protecting the underwriters for all of the materials in
8 the transactions and for anything Duke did wrong. And
9 the only thing that the underwriters indemnify the
10 Company for, if you read the underwriting agreement, is
11 the interest rate on the bonds, the names of the firms
12 underwriting, and the amounts that they underwrote.
13 That's it.

14 Anything that the underwriters have done in
15 the sales and marketing, if they did something wrong,
16 they did something that affects -- they're not
17 indemnifying the Company. So the fees associated as
18 part of the compensation. It's also the sales and
19 trading afterwards. It's meeting different client
20 needs. And so you got to balance those interests.

21 In my testimony, we talked about how there
22 was a balance of interest -- of self-interest in
23 checks. In the traditional debt, the Commission has
24 ongoing review so that there can always have a check if

1 they found out something else was done untoward or
2 there was inefficiency. Here, the Commission has to
3 give up all of that authority. So we're just saying
4 this is something different.

5 And the same thing with the certification,
6 Mr. Jeffries. I certainly believe that the fact that
7 the Company will certify to something and have their
8 opinion doesn't mean that they are violating law, they
9 might just have a different opinion. They might think
10 that that -- they would be very truthful in saying it's
11 their opinion that that's the lowest cost. We might
12 have a different opinion, and somebody else might have
13 a different opinion. That's what makes a market.

14 What you want to do is try to get what we got
15 in Florida where we got all the opinions lined up,
16 particularly the book runners and an independent
17 advisor. We didn't really ask for an opinion from Duke
18 in that, because it would be sort of a
19 self-certification, which we didn't think was important
20 as much as from the book runners and from an
21 independent evaluation. So those fees, yes, part of
22 it, but it's not the same sort of relationship as a
23 service provider, and a consultant, and advisor gives
24 for their -- to their clients.

1 And as you know, this has been a big debate
2 in the industry, it's like, when you talk to your
3 broker dealer, is he an advisor that sells to you or
4 not? Does he have to act in your best interest?
5 There's been a big debate about the best interest rule
6 on Wall Street. Wall Street has pushed back about
7 wanting that to be enforced, because they say
8 arms-length transaction.

9 So we're just bringing all these different
10 things together in this transaction and just trying to
11 make it all work in a cooperative and collaborative
12 way. And I think, as Mr. Schoenblum said in his
13 summary, you know, you don't need to fiddle with
14 success. Something that worked in Florida, we think
15 can work here.

16 Q. So, Mr. Fichera, is Saber Partners being
17 compensated for their participation in this evolution
18 that we're currently undergoing?

19 A. Yeah. We're being paid for our services, for
20 our advisory services, as we've been paid in other
21 transactions as well.

22 Q. And if you were centrally involved in the
23 structuring marketing issuance of these bonds, that
24 would be additional work, would it not?

1 A. It would be additional work. We're not being
2 paid out of the bond proceeds. We're being paid out of
3 a public -- specific statute that allows staff to have.
4 And, you know, if we do additional work, yes, we get
5 additional -- we have additional compensation.

6 Q. You think -- so your opinion is you're not
7 being paid out of the bond proceeds; is that correct?

8 A. That is correct.

9 Q. Who is paying your invoices right now?

10 A. I believe Duke Energy is paying them, but
11 it's under a different statute. It is not under the
12 storm securitization statute. I believe the public RFO
13 related to this transaction, the -- let me just pull it
14 up, I can give you the specifics. Under North Carolina
15 Statute 62-15(h) in the hole. It's based on that
16 compensation. So it's not based on the storm
17 securitization statute, and therefore not proceeds.

18 Q. So, Mr. Fichera, is it your opinion that the
19 interest that Saber has and the additional work that
20 they would do if the Public Staff's suggestion were
21 adopted by the Commission in this proceeding, that that
22 financial interest doesn't create any conflict of
23 interest between Saber and ratepayers?

24 A. No, sir, I don't think it does, nor does the

1 fact of you giving -- of counsel giving its opinions
2 and doing its work on the transaction creates a
3 conflict of interest with your client. You're doing
4 work for your client, and as long as you're putting
5 your client's interest first, that's what you got to
6 do.

7 Q. All right. Thank you, Mr. Fichera.

8 A. I don't think you'd be working -- I don't
9 think counsels that are going to be working on the
10 documentation or rest on the deal have a, quote,
11 financial interest in the deal, they're doing work for
12 their clients. If there's something different I'm
13 missing, I want to know.

14 Q. Now I'm gonna go back to Mr. Maher at this
15 point. Mr. Maher, on page 19 of -- lines 8 through 9
16 of your testimony, you state that in the context of
17 issuing storm recovery bonds, that the Company's main
18 motivation is to receive the debt proceeds in a timely,
19 efficient manner; is that right?

20 A. (Brian Maher) Yes.

21 Q. Can you -- is that a presumption on your
22 part? I mean, you don't have, like, an email from
23 Mr. Heath to his boss saying that's our main motivation
24 or anything like that, right?

1 A. I have no idea. I haven't seen anything like
2 that, yes. But it's a production -- a presumption that
3 Duke would like to do this transaction, recover the
4 billion dollars, let the bonds then pay themselves so
5 they could pay the ratepayers, then use the billion
6 dollars for other purposes, yes.

7 Q. Thank you. On page 19 of your testimony,
8 lines 9 through 12, you discuss the rationale as to why
9 you don't believe that DEP and DEC share the same
10 incentives to achieve the lowest cost of funds. Do you
11 see that?

12 A. Yes.

13 Q. And you state, and I'm gonna quote here:

14 "If I were going to borrow money and someone
15 else agreed to repay it for me, then I would
16 not be as concerned about the interest rate
17 and other terms of the loan as I would be if
18 I were on the hook to repay the loan myself."

19 So are you saying you would be okay with
20 letting the person who agreed to repay your loan pay
21 more than was necessary? I've only known you for a
22 short time, Mr. Maher. You don't seem like that kind
23 of guy.

24 A. No, I never want anybody to pay more than

1 necessary. The real question is how hard I would work
2 on something if someone else was gonna repay my debt as
3 opposed to whether it was coming out of my own bank
4 account.

5 Q. Right. So would you have a different
6 approach if you had a standard that was established by
7 statute in negotiating the loan? Would that cause you
8 to be more concerned about what the terms were?

9 A. If I had a standard, I would for sure abide
10 by that standard as I interpret it. I think we had
11 this discussion on what we mean by market conditions at
12 the time, and so I -- I might find a different standard
13 of market conditions at the time than if I were
14 responsible for this. In which case I would say I'm
15 gonna get the absolute lowest, and I'm gonna get the
16 underwriters to take some of the bonds if I think it's
17 gonna get me a lower price. I wouldn't just wait for
18 the all the investors to be found and what they were
19 gonna pay.

20 Q. Okay. Would you agree with me that the
21 transaction we're currently talking about, that there
22 is a statutory performance standard to obtain the
23 lowest storm charge?

24 A. Honestly, that's not my area of expertise,

1 but if you want me to say more about it, you could.

2 Q. Well, did you hear Mr. Heath testify
3 yesterday that there is a lowest cost standard and that
4 the Company agreed to it and that he would -- or that
5 the Company would certify that the standard was met as
6 part of the IAL process, and that ultimately the
7 Commission would have to approve that certification in
8 order to go forward with the bond; did you hear him
9 testify to that?

10 A. Yes, I did hear that.

11 Q. Thank you.

12 A. And I guess that is -- that's why I actually
13 feel the way I do, because I -- not disparaging him,
14 and I think he's -- as I said, I think he's a very
15 competent person. I think he has maybe a lower hurdle
16 for what the lowest cost standard is as defined by how
17 he defines you would price the bonds. So I think he
18 would call that lowest standard, and I can't argue if
19 that's what he calls lowest standard, but what I call
20 lowest standard is a more aggressive standard.

21 Q. All right. Thank you. With respect to
22 certification, I would like to read you a statement,
23 and it's short, it's only about 15 words, but I'd like
24 to -- maybe 20 -- read you a statement and ask you

1 whether you agree with the statement or not. And this
2 is the statement:

3 "When a person is required to pledge
4 something in writing rather than just orally
5 and has to account for results later, that
6 person is more likely to take that pledge
7 seriously."

8 A. Yeah, I would believe that that is true, yes.

9 Q. That's good, because that statement comes
10 from your testimony on page 22 --

11 A. Okay.

12 Q. -- lines 4 through 7. So I'm glad --

13 A. Sounded familiar. Sounded familiar. Thank
14 you.

15 Q. All right. Good.

16 A. (Joseph Fichera) Your memory isn't going.

17 Q. That was a cheap trick on my part, I
18 apologize.

19 MR. JEFFRIES: That's all the questions
20 I have for Mr. Maher. Thank you, sir.

21 Guess we're going to continue with cross
22 at this point of the panel; is that correct,
23 Chair Mitchell?

24 CHAIR MITCHELL: That is correct.

1 MR. JEFFRIES: All right. Then, at this
2 time, I'm gonna hand the mike over to Ms. Athens.
3 I think she's got some questions for
4 Mr. Schoenblum.

5 CHAIR MITCHELL: All right, Ms. Athens.

6 CROSS EXAMINATION BY MS. ATHENS:

7 Q. Good morning, Mr. Schoenblum. How are you
8 today?

9 A. (Hyman Schoenblum) Good morning, Ms. Athens.
10 Great.

11 Q. Good. So I'd like to start on pages 22 to 23
12 of your testimony, and I think you answered a similar
13 question that Mr. Sutherland did in your testimony.

14 Should the Commission give the Companies
15 broad flexibility to establish the final terms and
16 conditions of the bonds; is that right?

17 A. That's correct.

18 Q. And similar to Mr. Sutherland, your answer to
19 that question was also no, right?

20 A. That's correct.

21 Q. In responding to the question in the
22 negative, are you suggesting that the Company shouldn't
23 have flexibility to address market conditions at the
24 time of the bond issuance?

1 A. Is your question whether the Companies should
2 not have flexibility?

3 Q. My question was, in answering no to that
4 question in your testimony, are you suggesting that the
5 Companies should not have flexibility to address market
6 conditions at the time of the bond issuance?

7 A. No, I'm not entirely suggesting that.
8 Obviously, any issuer needs to have some flexibility.
9 But at the same time, this is the first securitization
10 issue for both of these companies, and they might not
11 be totally familiar with all of the aspects of
12 securitization, whether it's, you know, documentation,
13 market pricing, type of investors that invest in these
14 type of securities. So, yeah, flexibility is okay, but
15 at the same time, there are other factors that come
16 into play that may work to limit that flexibility.

17 Q. So if the Public Staff were to have
18 decision-making on a bond team and in some way overrule
19 the Companies, you would agree with me that that would
20 be limiting the Companies' flexibility?

21 A. The Public Staff -- our position is that the
22 Public Staff should be part and parcel of the bond
23 team, and the Public Staff -- and its advisor will have
24 the ability to review, analyze, do due diligence on all

1 aspects of the bond issuance. And so Public Staff is
2 going to make recommendations to the Company and to the
3 Commission as to what its position is and whether it
4 feels that the Companies are getting the best deal and
5 offering the best protection for ratepayers in this
6 transaction.

7 Q. Thank you. Do you have a copy of the
8 securitization statute in front of you?

9 A. Yes, I do.

10 Q. All right. I'd like to turn to Section
11 (b)(3)(b)(8). That should be page 5.

12 A. Page 5?

13 Q. Yes. And I'm looking at number 8 towards
14 the bottom.

15 A. Okay.

16 Q. And would you agree with me that it's a
17 requirement that Commission include in the financing
18 order that the flexibility to be granted to the public
19 utility in establishing the terms and conditions of the
20 storm recovery bonds, including but not limited to the
21 payment schedule, expected interest rates, and other
22 financing costs?

23 A. Yes, that's what the section says, and that's
24 what it reads. But as I explained earlier, there are a

1 lot of other factors involved that may work towards
2 limiting that flexibility, and all we're suggesting is
3 that the utilities not necessarily be the only body
4 making these decisions, and that Public Staff and its
5 advisors be part of the due diligence process to ensure
6 that the deals are the best deals and that the
7 ratepayers are getting the best transaction.

8 Q. So would you agree with me, though, that the
9 statute does not grant the Public Staff or its
10 financial advisors any flexibility?

11 A. I wouldn't read it quite that way, because if
12 you look at the -- at the provisions establishing the
13 Public Staff, which is the Section 62-15 of the public
14 service law, there are indications therein that the
15 Public Staff can have a role in evaluating financings
16 of the utilities in North Carolina. So they can play a
17 role, in addition to the utilities.

18 Q. But the statute does not specifically grant
19 or make a requirement that the Commission must include
20 in the financing order a section on the degree of
21 flexibility to be afforded to the Public Staff in
22 determining the terms and conditions of the storm
23 recovery bonds?

24 A. Well, these are the statutes relating to the

1 storm recovery costs, but it was our recommendation --
2 and the lead-in to this section talks about the
3 financing order. And the -- and what we're
4 recommending is that the financing order be more
5 inclusive and include the Public Staff and its advisors
6 as part of the process in doing the due diligence and
7 evaluating these transactions in addition to the
8 Companies.

9 Q. So would you agree with me that granting the
10 Companies some flexibility can be to the benefit of
11 customers?

12 A. I can agree with that statement in its
13 broadest terms, yes.

14 Q. And is one of your best practices that you
15 list on page 52 to ensure that all statutory limits
16 that benefit customers are strictly enforced?

17 A. Page 52?

18 Q. Yes, sir. Number 3 of your list of best
19 practices.

20 A. That's correct. That's what it says, yes.

21 Q. So why would we not strictly enforce this
22 provision of the statute and grant the public
23 utilities' flexibility in establishing the terms and
24 the conditions of the bonds?

1 A. As I said a moment ago, our recommendation is
2 that the financing order include other parties that
3 ought to be included in this process -- in the due
4 diligence process. So if the Commission accepts that
5 and issues a financing order that does that, then that
6 will be part of the -- that will become part of the
7 statutory limits that are to be enforced in this
8 proceeding.

9 Q. So is it your testimony that limiting the
10 Company's flexibility would not be inconsistent --
11 otherwise inconsistent with the statute?

12 A. In a broad sense, that's probably true. But
13 again, our recommendation is that the financing order
14 should be more expansive and include other parties
15 besides the utilities in the process.

16 A. (Joseph Fichera) And I think one of the
17 issues here -- none of us are all lawyers here, so I
18 think really we're talking -- it seems we're talking
19 past each other about what the definition of
20 flexibility is. I probably hung around more lawyers
21 than the rest of my team on these issues. I think
22 we're talking about establishing a process where there
23 is flexibility that the Company has, but through an
24 established process that has these things go forward.

1 And with the Commission always being the decision-maker
2 in the end.

3 So we don't think that a bond team process --
4 I think that those words flexibility are in almost
5 every statute that we've dealt with that has a -- I
6 think there was certainly in Florida and elsewhere. So
7 that there -- it's part of a process, and that's part
8 of the flexibility. The one thing I can tell you about
9 the North Carolina statute that is different than any
10 other securitization statute over the past 23 years was
11 that it authorized Public Staff, the independent agency
12 in the Commission, in addition to the Commission, to
13 hire independent advisors, consultants to be paid out
14 of proceeds.

15 That seemed -- we sort of looked at that as a
16 unique thing that the legislature was saying that
17 Public Staff was going to be part of the transaction,
18 because Public Staff had authorization to be part of
19 the financing costs. So if you go to the definition of
20 financing costs -- and this is where I've spent too
21 many time with lawyers -- and you say what the
22 financing costs are, and then Public Staff is, and then
23 you go to the legislative fiscal report about what that
24 meant in terms of the -- so you sort of put all those

1 together, you see that -- you see the Public Staff
2 should be involved. And then, in our testimony, we're
3 just describing a process that affords the Commission
4 ultimately decision-making authority and it also gives
5 the Company flexibility.

6 They're proposing different things to be
7 done, but there's a cooperative and collaborative
8 effort that comes together. And I've never seen a
9 situation where we've been in where somebody -- we
10 overruled something. I don't think that would --
11 that's not the -- it works on a consensus basis. So
12 everybody comes together with that, and that's the best
13 transaction, is where we have agreement, we go forward,
14 independent verifications, and then the Commission
15 decides yes, no.

16 Q. Thank you, Mr. Fichera. And I'm gonna turn
17 back to Schoenblum now.

18 In sticking with the statute, would you agree
19 with me that the statute defines assigning (sound
20 failure)? And that would be on page 1 of the statute.

21 A. (Hyman Schoenblum) I'm sorry, I lost you.

22 MR. CREECH: We lost your sound there.

23 THE WITNESS: We lost your sound there
24 for a moment. Can you repeat that, please?

1 Q. Can you hear me now?

2 A. Yes.

3 Q. So looking on page 1 of the statute, would
4 you agree with me that the statute defines the term
5 "assignee"?

6 A. I see that. That's sub number (2), (a)(2);
7 is that what you're referring to?

8 Q. Correct.

9 A. I see that.

10 Q. And would you agree with me that the statute
11 goes on to define the term "bondholder"?

12 A. That's subsection (2)(a). I see that.

13 Q. And would you agree with me that the statute
14 goes on to define the term "financing party"?

15 A. You're referring to subsection (4)?

16 Q. Yes, sir.

17 A. I see that. I haven't read it, but I see
18 that.

19 Q. And does it go on to also define the term
20 "Commission"?

21 A. Which section are you referring to? Sorry,
22 oh, above that, subsection (3).

23 Q. I believe it's (a)(5).

24 A. (A)(5)? One second. (A)(5), it says

1 "financing order."

2 Q. Are you looking on the first page? And would
3 you agree with me that on the first page, the statute
4 defines the term "Commission"?

5 A. The word "Commission" is defined in (a)(3) as
6 the North Carolina Utilities Commission. That's what I
7 see.

8 Q. But the statute does define the term
9 "Commission"?

10 A. That's correct.

11 Q. And does the statute also define the term
12 "public utility"?

13 A. That's, I believe, subsection (9), public
14 utility.

15 Q. So would you agree with me that the statute
16 does not define Public Staff?

17 A. Well, again, I would refer back to 62-15,
18 which lays out the duties and requirements for the
19 Public Staff. And the first sentence of 62-15(a) says:

20 "There is established in the Commission the
21 office of executive director, the salary and
22 longevity pay" --

23 Et cetera, and that talks about the -- and
24 that's the requirement for the Public Staff.

1 Q. But you --

2 A. When I first saw that, and I looked at the
3 wording here, and it said "in the Commission," it kind
4 of led me to believe that the Public Staff was almost
5 sort of an extension of the Commission.

6 Q. Thank you. Are you aware that the Public
7 Staff is actually a separate and independent agency of
8 the Commission?

9 A. That's -- that's -- that's my understanding,
10 yes.

11 Q. And looking back to the statute, you would
12 agree that 62-172 does not define Public Staff, or
13 consultant, or financial advisor, but it does define
14 Commission and public utility?

15 A. That's correct.

16 Q. Thank you. I'd like to turn to your time at
17 Consolidated Edison of New York, which I'll refer to as
18 Con Ed if that's okay with you.

19 A. Sure.

20 Q. So looking to page 9 of your testimony, you
21 state that you met very frequently with institutional
22 investors, fund managers, stock and bond research
23 analysts, and the media to present Con Ed's financial
24 position to the investment community; is that correct?

1 A. That's correct.

2 Q. When you met with these people, you met with
3 them on behalf of Con Ed or possibly Con Ed's
4 subsidiaries; is that correct?

5 A. That's correct.

6 Q. And were these meetings in the capital
7 markets authorized by Con Ed or the applicable
8 subsidiary company?

9 A. That's correct.

10 Q. And when working at Con Ed, did you ever
11 participate in an offering of registered securities by
12 Con Ed or one of its subsidiaries?

13 A. Yes, I did.

14 Q. And did you speak with the investors during
15 the marketing of these securities?

16 A. When I was treasurer, I was part of a team
17 that marketed to securities, to potential investors.

18 Q. And did that team include anyone who was not
19 working on behalf of Con Ed?

20 A. It included Con Ed representatives and
21 underwriters that may have been employed by Con Ed.

22 Q. And while working at Con Ed, are you aware of
23 an occasion when someone other than the issuer or the
24 underwriter had conversations with investors in a

1 registered securities offering?

2 A. Not to my knowledge.

3 Q. And more specifically, are you familiar with
4 any utility securitization completed by a Con Ed
5 subsidiary?

6 A. There was a limited securitization done by
7 one of Con Ed's subsidiaries that was based in
8 New Jersey.

9 Q. And did Con Ed ever authorize an intervenor,
10 including but not limited to a consumer advocate state
11 agency, in -- group in New Jersey to speak with
12 investors during the offering of those securities?

13 A. To the best of my knowledge, none was
14 requested.

15 Q. In that securitization, did a state agency,
16 other than the New Jersey Utilities Commission, have
17 decision-making?

18 A. There were probably other intervenors in the
19 proceeding, but, of course, the New Jersey Commission
20 made the final decisions.

21 Q. Did the New Jersey Utilities Commission make
22 any decisions with respect to the bond issuances after
23 the financing order was issued?

24 A. One second. I'm just reading my response to

1 interrogatory 2-42 which discusses this subject.

2 Can you repeat the question, please?

3 Q. Did the New Jersey Public Utilities
4 Commission have decision-making authority once the
5 financing order for that securitization was issued with
6 respect to the issuances of the bonds?

7 A. I do not recall how that played out. Whether
8 the Commission made any final determination in that
9 proceeding, I do not recall. I would assume they did,
10 but I can't say definitively.

11 Q. Can you recall whether there was a bond team
12 at all?

13 A. There was no bond team in that proceeding.
14 It was a very small issuance. I think it was about
15 \$40 million or thereabouts. It was a very small
16 securitization, limited securitization.

17 Q. But regardless of size -- regardless of size,
18 it was a utility securitization similar to the one that
19 Duke Energy Carolinas and Duke Energy Progress are
20 proposing in this proceeding; is that correct?

21 A. Yes, it was, and there was no bond team. In
22 fact, the whole concept of the bond team has evolved
23 over the years as part of the work being done to
24 establish best practices. So while there was no bond

1 team in that proceeding, I would suggest that the
2 concept of the bond team has come about as a result of
3 trial and error over the years. And my experience with
4 securitization in the Florida transaction, to me that
5 was sort of the first transaction that I was intimately
6 involved in. And I was surprised by the complexity of
7 the transaction, and as such, I found that the bond
8 team added tremendous value to that process because of
9 the complexity of the issuance.

10 So there may not have been a bond team
11 involved in the Con Ed transaction, but that has
12 changed over the years, and the bond team has become
13 much more acceptable and recognized by everybody that
14 it adds value to the process.

15 Q. So even though that transaction did not
16 include a bond team, was that securitization
17 successful?

18 A. I'm not sure how you measure success. If
19 your measure of success is the lowest cost, I'm not
20 sure that I know the answer to that.

21 Q. Did you say that there were any rate -- I'm
22 sorry?

23 A. We didn't have any metrics to measure the
24 concept of lowest cost as we do today. I'm sorry.

1 Q. So would you say that there were, in fact,
2 ratepayer savings, though, that resulted from that
3 securitization?

4 A. Absolutely there were ratepayer savings, but
5 I can't assure you -- I cannot assure you that they
6 were the maximum ratepayer savings that could have been
7 realized had there been a bond team, for example.

8 Q. But you would agree with me that that
9 transaction went through and did result in customer
10 savings, despite there not being a bond team
11 whatsoever?

12 A. That's correct.

13 MS. ATHENS: No further questions for
14 the witness.

15 CHAIR MITCHELL: Okay. Just so I'm
16 clear, Ms. Athens and Mr. Jeffries, does that
17 conclude Duke's cross examination of the panel?

18 MR. JEFFRIES: No, Chair Mitchell. We
19 have cross examination for Mr. Fichera.

20 CHAIR MITCHELL: Okay. Proceed, please.

21 MR. JEFFRIES: All right. Thank you.

22 CROSS EXAMINATION BY MR. JEFFRIES:

23 Q. Mr. Fichera, in your summary you cited to the
24 DEF bond issuance in Florida as an example of your

1 prior work in this area; is that correct?

2 A. Yes, sir, I did.

3 Q. Okay. And you represented -- and I say
4 you -- Saber represented the Florida Public Service
5 Commission in that transaction, right?

6 A. Yes. We were hired by them to represent
7 ratepayers in the transaction, yes.

8 Q. Okay.

9 A. Ratepayers.

10 Q. The contract was with the Commission,
11 correct?

12 A. Yes. The Commission's staff. And I think
13 they have separate staff from -- to support just the
14 Commissioners, and then there's the general staff. And
15 I think we were the general staff.

16 Q. Okay. Thank you. You did not represent the
17 office or work for the office of public counsel in
18 Florida in that transaction, did you?

19 A. No. They were not like Public Staff is here
20 in the Commission. They were a separate entity.

21 Q. Mr. Fichera, you've presented on
22 securitization to various groups, including the
23 national association for SUCA, so what is that?

24 A. State Utility Consumer Advocates.

1 Q. Okay. Okay. Do you have our DEC/DEP Cross
2 Exhibit Number 6 handy?

3 A. I know where I can get it.

4 Q. Yeah. That would be great if you wouldn't
5 mind.

6 A. What is it?

7 Q. It's your presentation to SUCA from last
8 year. You may have it memorized. You may not need to
9 look at it to respond.

10 A. Yeah, why don't we just go through it, if I
11 need to look at it?

12 Q. Okay. Great. You have a slide in there and
13 it's --

14 MR. CREECH: Excuse me, Mr. Jeffries, my
15 apologies. If I may, I do want to get this in
16 front of Mr. Fichera. Mr. Fichera, you do have it,
17 obviously, and I emailed it again to you.

18 THE WITNESS: That's their cross?

19 MR. CREECH: That's right. Number 6.

20 THE WITNESS: Okay. Let me --

21 MR. CREECH: If that's okay,
22 Mr. Jeffries, yeah?

23 MR. JEFFRIES: No, that's great. I
24 appreciate that. I think it's much better if he's

1 got that in front of him.

2 THE WITNESS: Okay. It's --

3 MR. CREECH: It's premarked Exhibit
4 Number 6.

5 THE WITNESS: Yes, I see it. Double
6 pages?

7 Q. Exactly.

8 A. Copyrighted. Did you pay a fee for this or
9 no?

10 Q. I have no knowledge where this came from, to
11 be honest with you.

12 A. Okay. Had to come from our website. I don't
13 know. We put a copyright on it because we're proud of
14 it.

15 Q. Yeah. Okay. Good.

16 MR. JEFFRIES: Chair Mitchell, we would
17 ask that this be marked as DEC/DEP Fichera Cross
18 Exhibit Number 1.

19 CHAIR MITCHELL: All right.

20 Mr. Jeffries, the document will be marked DEC/DEP
21 Fichera Cross Examination Exhibit Number 1.

22 MR. JEFFRIES: Thank you.

23 (DEC/DEP Fichera Cross Examination
24 Exhibit Number 1 marked for

1 Q. And it's -- it's relevant because it's --
2 this is the kind of transaction that we're talking
3 about right now in this proceeding, correct?

4 A. Yes. There's been a lot of interest over the
5 past 12 months with -- about bringing securitization,
6 not to just what traditional uses were, but things like
7 early retirement of coal plants and other sources, grid
8 modernization, things like that.

9 Q. Okay. Thank you. And so I've looked at
10 these core best practices, and as you say, they're the
11 best practices that can fit on one page.

12 But the first one, customer benefit, is
13 you're citing to the lowest cost standard for
14 ratepayers; is that right?

15 A. Yes. And notice that we also put in present
16 value savings because we think that's important. You
17 know, you might have a misinterpretation of the lowest
18 cost by just being the rate, for like a 15-year
19 mortgage has a lower cost than a 30-year mortgage, yet
20 a 30-year mortgage might save you more money over time.
21 So it's important to have the concept of present value
22 in addition to the word cost.

23 Q. Sure. Thank you. On the second is a
24 reference to the authority, and I've paraphrased that

1 is the ability of the Commission to include ratepayer
2 protective measures in the financing order.

3 Do you agree that that's what that second
4 best practice is addressing?

5 A. Yes. The Commission needs -- who is going to
6 be the ultimate decider here, and it needs to have the
7 flexibility not restricted by the legislature to do its
8 duty to protect, you know, the public interest by being
9 able to put terms and conditions that it determines is
10 appropriate through the appropriate procedures, like
11 we're going through now, through a hearing and other
12 things like that, and taking testimony, stuff like
13 that.

14 Q. Okay. I'm not gonna ask you any specific
15 questions about these last three, but, I mean, they
16 basically -- and I'm paraphrasing here, and let me know
17 if you think I got it wrong, but the third is that you
18 think ratepayers ought to have representation and
19 structuring marketing pricing with the bonds. The
20 fourth is that the Commission should have access to
21 expert resources. And the final one is that there
22 ought to be a certification of lowest costs.

23 Do you agree with that?

24 A. Yes. And it's important to note that the

1 nuances there that are substantive, which is that there
2 are multiple certifications that should line up in the
3 financial markets. You always get a second opinion.
4 If a company is acquiring another company, they have an
5 opinion, and the acquired company gets an independent
6 opinion to verify. So yes, that's your sort of summary
7 there, but those specifics -- I shouldn't say nuances,
8 they're substantive -- are important to it.

9 Q. Sure. Now, these best practices that you've
10 got listed, these are, I guess I would call a Saber
11 construct; would you agree with that?

12 A. No. I think we've developed them -- you
13 know, it was interesting, somebody else talked to me
14 and said not everybody does this. And they said, well,
15 that's why they're called best practices, because
16 they're relative to how other people have done and what
17 we've seen over time. For example, prior to the Texas
18 transactions, which Becky Klein talked about, of the
19 \$50 billion that was issued, \$21 billion was issued
20 without any Commission involvement whatsoever.

21 Texas started that process and then suddenly
22 others started picking up. New Jersey had an
23 independent financial advisor, Bear Stearns. Not me.
24 I wasn't there at the time. And then other states.

1 And then Louisiana, and then Wisconsin, then
2 California. And so I think, as Hyman Schoenblum said,
3 these have evolved over time from what people have
4 done, and we've been probably -- since we've done the
5 most transactions over the past 20 years as an
6 independent advisor, they get associated with us, but I
7 think other people have used them.

8 Q. So I think, actually, I was asking a little
9 simpler question. You may have just answered it.

10 I mean, these -- these -- whether they're
11 used by other parties or not, these are your best
12 practices, right? I mean, you -- you came up with
13 these. You're the one that decided based upon your
14 experience that these are, in your mind, best
15 practices, right?

16 A. In my mind? I think we've testified,
17 Mr. Sutherland, is that by examining outcomes of other
18 transactions and what has worked and what hasn't
19 worked, we've come to the conclusion that these are the
20 best practices and have given testimony to that fact.
21 They're not figments of our mind. They're the results
22 of analysis of transactions over time. And
23 consultations with other people like, you know,
24 Bill Moore, the former CEO, treasurers, other people

1 who've been in the capital markets and involved with
2 these.

3 Q. You know, it's rare to find someone who won't
4 take credit for something that they've created, but let
5 me try it another way.

6 A. I can't take credit for certain -- the notion
7 of an independent certification is not -- I didn't
8 develop it. It's just been applied here.

9 Q. Okay. You didn't draw these, there's not
10 some NARUC resolution out there saying these are the
11 best practices when you engage in a securitization
12 transaction, or some NASUCA resolution, or some
13 independent third party academic discussion that
14 identifies these; you're not aware of anything like
15 that, right?

16 A. No, I'm not aware of those kinds of formal
17 endorsements of best practices in the market, no. I
18 don't think anywhere has that. I don't think the legal
19 profession, or the accounting profession, or anything
20 else has, sort of, something written down as best
21 practices.

22 Q. So, Mr. Fichera, Duke has, as part of their
23 filing -- initial filing and direct testimony, they've
24 basically said to the Commission, we know how to issue

1 bonds, and we believe our interests are aligned with
2 customers. And I know that you may not agree with that
3 second point necessarily, but Duke's --

4 A. Don't assume that I don't agree with that. I
5 do agree. They have some certain experiences and such.
6 I wouldn't make the conclusions. Why don't you ask me
7 the question?

8 Q. Okay. Well, I was getting there. But then
9 in their rebuttal testimony -- and so in their initial
10 proposal to Commission, they basically said we can do
11 this. They pointed out that the statute doesn't have
12 any express directive for the Commission or the Public
13 Staff to be involved, post financing order. But then
14 in their rebuttal they came back and said, you know,
15 we're okay with a bond team approach. It's a different
16 bond team approach than the Public Staff has, but --
17 and Mr. Heath said it yesterday, we have no problem
18 with Commission being a co-equal decision-maker on a
19 bond team, if the Commission decides that that's the
20 role they want to pursue.

21 Do you agree that, if the Commission had a
22 representative on the bond team with co-equal
23 decision-making authority, that they would be able to
24 inform themselves as to whether the bonds were going to

1 be issued consistent with the lowest cost standard for
2 ratepayers?

3 A. Yes. And the Commission could do this on
4 their own with access to the proper expertise. It's
5 not something they do consistent with other things they
6 do. And the reason why the Florida Commission and
7 others came -- and came to us was they knew it was
8 outside of their normal course of work and that they
9 needed individual expertise that was specifically
10 focused on this. So the Commission can do this on
11 their own.

12 Public Staff just -- I think the Public Staff
13 proposal that you're referring to coming out of our
14 testimony is simply adapting to the unique aspects of
15 North Carolina that has this entity called the Public
16 Staff in the Commission as an independent agency, but
17 also was authorized by the Legislature to engage people
18 as a financing cost and have a duty to intervene.

19 So when we looked at their RFQ from Public
20 Staff as it came out and familiarized this with us, we
21 thought -- the reason why we responded to it was, well,
22 this is consistent with sort of the staff that we
23 worked with in Florida, staff we worked with in Texas,
24 the staff we worked with in West Virginia, the staff we

1 worked in New Jersey, and didn't see this distinction
2 that seems to be going back and forth here between
3 counsels. You know, the difference between a Public
4 Staff and the Commission staff.

5 You know, we're not lawyers. You guys will
6 figure that out, but we think it's a distinction
7 without a difference. The Commission can do it or the
8 Public Staff can do it. The Commission can do it by
9 relying on the Public Staff. Certainly the Commission
10 can do it on their own if they want to, and we'd be
11 happy to work with the Commission.

12 Q. So, in your mind, there's no difference
13 between the Commission and the Public Staff; is that
14 what you're saying?

15 A. No, there's clearly a difference. I mean,
16 the Commission is the ultimate decision-maker. The
17 Public Staff is more of an advisor in -- now, the legal
18 term is intervenor in that case, in rates and such.
19 And the ratemaking process here goes from the financing
20 order all the way to the pricing. So the notion of
21 having the Public Staff simply in a post-financing
22 order process, pre-issuance process, continuing to be
23 involved in the ratemaking, we thought -- you know,
24 we're not lawyers -- is that it's consistent with the

1 legislative mandates of the Public Staff, and the
2 Commission is the ultimate decider. Public Staff
3 wouldn't be deciding anything.

4 So the Commission staff would be deciding --
5 I mean, the Commission decides we like this or we
6 don't. The bond team -- and I think this is where some
7 confusion might be coming, because when we say a joint
8 decision-maker on the bond team. Well, the bond team
9 is simply coming up with a structure, a marketing plan
10 and coming, and then that would be presented to the
11 Commission to make the decision. And having two people
12 of equal decision-making authority sort of forces a
13 consensus to be made.

14 Now, we know, in real life, that we can't
15 always agree on something. So we said that part of the
16 process is you have a designated Commissioner to be a
17 tiebreaker of that specific decision that couldn't be
18 agreed to. And then that would go forward, and then
19 the Commission makes the final decision. Do I accept
20 that or do I not? So there's no, like, delegated
21 authority to an individual Commissioner to decide
22 anything, because it's always the full Commission
23 making the decision of whether to accept or reject a
24 transaction or tell you guys can go -- go -- you guys

1 keep negotiating and come back with a joint stipulation
2 for me that I can accept or reject. Something like
3 that.

4 So it's -- and that's sort of the process
5 worked in Florida and why we mentioned it, is -- and we
6 were very pleased to hear Tom Heath's testimony
7 yesterday, because adopting the corporate bond index,
8 the bond team, that was not the initial application of
9 Duke Energy Florida before the Florida Commission.
10 That came after our testimony similar to here in which
11 we proposed the bond team, and then came after a
12 negotiation that then agreed to a joint stipulation
13 that had all these things and that we ultimately did.

14 So the fact that now Duke is adopting that is
15 very -- I will take credit for that. Adopting those
16 things was very satisfactory to us, but now they were
17 making some hyper-technical distinctions between Public
18 Staff and Commission staff. We leave that up to the
19 Commission to decide. And we could work for the
20 Commission or we could work for Public Staff in
21 providing that in that point, the written
22 certifications and bring our experience to it.

23 So I think that -- that's where I think some
24 confusion in this discussion. We clearly see the

1 Commission is the decision-maker. Public Staff is --
2 Public Staff would be helping put together the
3 transaction, and then the Commission votes. That's how
4 it was done in Florida, it was also how it was done
5 elsewhere, but let's just focus on Florida because
6 that's where Tom Heath and I traveled around the
7 country together talking to investors, and -- on a road
8 show, and it worked very successfully.

9 Q. Well, so it's interesting to me. We've had
10 some testimony from Mr. Heath yesterday about Florida,
11 and now we've had some testimony from you and some of
12 the other folks from Saber about Florida today. And I
13 think there's two things I get from it is that Duke has
14 obviously said they're comfortable with the Florida
15 model, and you obviously say you're comfortable with
16 the Florida model, but I don't think we're talking
17 about the same thing.

18 A. I think we're talking about the same thing,
19 but Duke is comfortable with the Florida model as long
20 as Saber Partners isn't involved, I think is where we
21 disagree. But the model is about the staff, and now
22 we're getting into the discussion between Commission
23 staff and Public Staff. I know you brought up OPC, the
24 Office of Public Counsel, but they're not the same as

1 Public Staff here. This is not the same. They're not
2 funded, they're not in the Commission, they're apart.

3 You know, I think we tried in our best to
4 adapt to the specific unique situation of
5 North Carolina, which seem -- which has Public Staff.
6 The Commission didn't do an RFQ. I think that they
7 were aware that staff was doing an RFQ for advisors.
8 We looked at it. We thought this was consistent with
9 our business practices where we worked with other
10 Commission staff. And as Hyman pointed out, you read
11 the statute that says an independent agency in the
12 Commission, and now we're -- I'm just a little confused
13 about why we're debating over what the definition of
14 staffs are.

15 The key point is a ratepayer representative.
16 If the Commission staff wants to do that right now
17 without Public Staff, they certainly can do it. We
18 recommend that they have independent expertise. We
19 would be available to do that. We don't think there's
20 any conflict of interest as Mr. Heath seemed to suggest
21 yesterday, because it's still the same model that
22 worked successfully in Florida.

23 Q. So I'd like to follow up real quickly on
24 something you just said regarding the Commission, if

1 they wanted -- their Commission staff wanted to do
2 this, then they would be fine with that.

3 And where I was ultimately trying to go here
4 was, if the Commission took it on themselves to play
5 the role that you've advocated, the role that the
6 Florida Public Service Commission did in Florida, that
7 that would check all of those five best practices that
8 are on your slide 26, correct?

9 A. In terms of -- I think if you look at the
10 financing order similar to the attached Florida
11 financing order and had all the representations and
12 descriptions and the certifications, mere Commission
13 involvement wouldn't do it. I think there's a lot of
14 other details that would be required. But the biggest
15 step is -- in this instance is someone representing the
16 ratepayers, however the Commission would like that to
17 be, whether it would like it to be its direct staff or
18 Public Staff, and having access to independent
19 expertise, and then with a duty to the ratepayer, and
20 then those written certifications from the book runner
21 and the underwriters and the independent advisor.

22 I have to tell you, we didn't ask for a
23 certification that Mr. Heath discussed that he's
24 willing to give here in Florida. The reason we didn't

1 ask for it, we didn't think it was that critical,
2 because it was more like a self-certification, which is
3 of limited value. It could be their very opinion, and
4 I don't want to -- there was some suggestion that -- I
5 think they could believe that that was the lowest cost.
6 And we're not saying that they're not gonna not comply
7 with the statute. They could truly believe that that
8 was the lowest cost. But could be a different view.
9 And we want to have them all lined up. And when you
10 start doing that, getting people the same, we need to
11 all agree.

12 Or, if we're gonna put a condition -- for
13 example, say I disagreed with something that Duke did,
14 I might condition that in my opinion and say "but for
15 this," we think they got that, and then let the
16 Commission decide. They can either go forward with the
17 transaction, even though an opinion was qualified, or
18 they could say, oh, no, we don't want to go forward.

19 Commission authority is paramount. How you
20 get them the best advice as to what the structured
21 marking and pricing ultimately produced, is this
22 process. And I agree with you, Mr. Jeffries, the
23 Commission staff can do it, or Public Staff, or the
24 Commission staff working through Public Staff. There

1 is a couple of different ways to doing it, as long as
2 there is someone representing the ratepayer fully armed
3 on the other side at the negotiating table, not outside
4 the room, you know, looking in or checking or anything.

5 Q. Mr. Fichera, do you have access to our
6 DEC/DEP Cross Exhibit 10?

7 CHAIR MITCHELL: All right.

8 Mr. Jeffries, I'm gonna stop you right now. We're
9 going on our lunch break, so we will resume with
10 your next line of questions when we return. We
11 will go off the record now and we will go back on
12 at 2:00.

13 (The hearing was adjourned at 12:20 p.m.
14 and set to reconvene at 2:00 p.m. on
15 Friday, January 29, 2021.)
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CERTIFICATE OF REPORTER

STATE OF NORTH CAROLINA)
COUNTY OF WAKE)

I, Joann Bunze, RPR, the officer before whom the foregoing hearing was taken, do hereby certify that the witnesses whose testimony appear in the foregoing hearing were duly affirmed; that the testimony of said witnesses were taken by me to the best of my ability and thereafter reduced to typewriting under my direction; that I am neither counsel for, related to, nor employed by any of the parties to the action in which this hearing was taken, and further that I am not a relative or employee of any attorney or counsel employed by the parties thereto, nor financially or otherwise interested in the outcome of the action.

This the 3rd day of February, 2021.

Joann Bunze



JOANN BUNZE, RPR

Notary Public #200707300112