PUBLIC STAFF – NORTH CAROLINA UTILITIES COMMISSION

DIRECT TESTIMONY OF THE PUBLIC STAFF

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

DOCKET NOS. E-22, SUB 551 AND G-5, SUB 585

September 26, 2018

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND PRESENT POSITION.

A. My name is Michael C. Maness, and my business address is 430 North Salisbury Street, Raleigh, North Carolina. I am the Director of the Accounting Division of the Public Staff. My qualifications and experience are provided in Appendix A.

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND PRESENT POSITION.

A. My name is Jan A. Larsen, and my business address is 430 North Salisbury Street, Raleigh, North Carolina. I am the Director of the Natural Gas Division of the Public Staff. My qualifications and experience are provided in Appendix B.

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND PRESENT POSITION.

A. My name is John R. Hinton, and my business address is 430 North Salisbury Street, Raleigh, North Carolina. I am the Director of the

Economic Research Division of the Public Staff. My qualifications and experience are provided in Appendix C.

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS, AND PRESENT POSITION.

A. My name is James S. McLawhorn, and my business address is 430 North Salisbury Street, Raleigh, North Carolina. I am the Director of the Electric Division of the Public Staff. My qualifications and experience are provided in Appendix D.

Q. PLEASE DESCRIBE THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING.

A. The purpose of our testimony is to present the results of the Public Staff's investigation of the application and direct testimony filed on January 24, 2018, and June 22, 2018, respectfully, by Dominion Energy, Inc. (Dominion Energy or Dominion) and SCANA Corporation (SCANA) (collectively, the Applicants), pursuant to N.C. GEN. STAT. § 62-111(a) for authority to engage in a proposed business combination transaction (Merger), whereby SCANA, the parent company of Public Service Company of North Carolina, Inc. (PSNC), will become a wholly-owned subsidiary of Dominion Energy pursuant to the Agreement and Plan of Merger (Merger Agreement) attached to the application as Exhibit 1; and to set forth commitments made by Dominion Energy and SCANA, and their public utility subsidiaries, Dominion Energy North Carolina (DENC) and PSNC, respectively, in Dominion's Regulatory Conditions and Code of Conduct. In our testimony, we describe the scope of the Public Staff's investigation of the proposed Merger; discuss the balancing of costs and benefits of the proposed business combination; discuss the rules governing affiliate transactions; describe the primary reasons for and major provisions of the Merger-related Regulatory Conditions and Code of Conduct recommended by the Public Staff, which are attached as Exhibit 1; and present the Public Staff's recommendation regarding the North Carolina Utilities Commission (Commission) approval of the transaction.

Q. PLEASE DESCRIBE THE PUBLIC STAFF'S INVESTIGATION.

A. A task force of accountants, engineers, attorneys, and financial analysts conducted an investigation of the proposed Merger, including the market power and cost-benefit analyses submitted with the application. The Public Staff submitted data requests to the Applicants and reviewed the responses to those data requests. The Public Staff also reviewed the Merger proxy statements and other documents filed by the Applicants with the Securities and Exchange Commission, and the Applicants' submissions to the Federal Trade Commission and the US Department of Justice pursuant to the Hart-Scott-Rodino Antitrust Improvements Act.

Q. WHY IS IT IMPORTANT TO IDENTIFY AND BALANCE THE COSTS AND BENEFITS OF A PROPOSED MERGER OR BUSINESS COMBINATION?

A. N.C. GEN. STAT. § 62-111(a) provides that no merger or combination affecting any public utility shall be made through acquisition or control by stock purchase or otherwise, except after Commission approval, which "shall be given if justified by the public convenience and necessity." This statute requires the Commission to review all aspects of a proposed merger and to balance all potential benefits and costs of the merger in determining whether the transaction should be approved. In reviewing applications for merger approval, the Commission has considered such factors as the maintenance of or improvement in service quality, the extent to which costs can be lowered and rates can be maintained or reduced, the extent to which the merger could have anticompetitive effects, the continuation of effective state regulation, and the relationships between and among the various units of the merged firm. In approving a merger application, the Commission has sought to ensure that the proposed transaction would have no adverse impact on the rates charged and the service provided to North Carolina jurisdictional ratepayers,1 that ratepayers were protected and insulated to the maximum extent possible from all known and

[1] Includes North Carolina retail electric customers of Dominion and North Carolina customers of SCANA.

potential costs and risks associated with the transaction, and that the benefits of the transaction to ratepayers were sufficient to offset those potential costs and risks.

As explained in the Order Approving Merger Subject to Regulatory Conditions and Code of Conduct, issued September 29, 2016, in Docket Nos. E-2, Sub 1095, E-7, Sub 1100, and G-9, Sub 682 (Duke/Piedmont Merger Order):

> In prior merger proceedings the Commission has established a three-part test for determining whether a proposed utility merger is justified by the public convenience and necessity. That test is (1) whether the merger would have an adverse impact on the rates and services provided by the merging utilities; (2) whether ratepayers would be protected as much as possible from potential costs and risks of the merger; and (3) whether the merger would result in sufficient benefits to offset potential costs and risks. See Order Approving Merger Subject to Regulatory Conditions and Code of Conduct (Duke/Progress Merger Order), issued June 29, 2012, in Docket Nos. E-2, Sub 998 and E-7, Sub 986, aff'd, In re Duke Energy Corp., 232 N.C. App. 573, 755 S.E.2d 382 (2014). These questions are related to one another and together establish a reasoned framework upon which utility mergers may be evaluated. In making these assessments, the Commission has also examined factors such as whether service quality will be maintained or improved, the extent to which costs can be lowered and rates can be maintained or reduced, and whether effective regulation of the merging utilities will be maintained. See Order Approving Merger and Issuance of Securities, issued April 22, 1997, in Docket No. E-7, Sub 596.

Duke/Piedmont Merger Order, p. 68.

Q. WHAT ARE THE REQUIREMENTS OF THE COMMISSION'S ORDER REQUIRING FILING OF ANALYSES, ISSUED NOVEMBER 2, 2000, IN DOCKET NO. M-100, SUB 129 (M-100, SUB 129 ORDER)?

A. The M-100, Sub 129 Order requires that merger applications be accompanied by a market power analysis and a cost-benefit analysis. The Applicants submitted both a cost-benefit analysis and a market power analysis with the application to comply with this requirement. In its *Order Scheduling Hearing, Establishing Procedural Deadlines, and Requiring Public Notice* issued on June 19, 2018, in the current proceeding, the Commission found and concluded that the application satisfies the requirements of the Order Requiring Filing of Analyses. An investigation and verification of the cost-benefit analysis and market power analysis is an essential part of the Commission's consideration of the proposed Merger and application of the statutory standard for approval. The Public Staff believes that the quantitative benefits of the Merger, together with strong regulatory conditions proposed by the Public Staff, are sufficient to meet that standard.

Q. PLEASE DESCRIBE THE PROPOSED TRANSACTION.

A. In accordance with the Merger Agreement, each issued and outstanding share of common stock of SCANA (other than the cancelled shares as defined in Section 2.01(b) of the Merger

Agreement) will be converted into the right to receive 0.6690 validly issued, fully paid and non-assessable shares of common stock of Dominion Energy. Based on SCANA's book value as of December 31, 2017, of $11.161 billion,[2] the purchase will result in an estimated $839 million acquisition premium.[3] This will be recorded at the Dominion Energy holding company level and will not impact DENC's or PSNC's financial statements. Upon the close of the Merger, SCANA will no longer be a publicly traded company, but will continue to exist as a wholly-owned direct subsidiary of Dominion. PSNC will remain a direct, wholly-owned subsidiary of SCANA, and is expected to retain its current name, corporate form and headquarters. The Applicants state that none of the acquisition premium costs will be passed on to DENC's or PSNC's customers

Q. PLEASE DESCRIBE PUBLIC SERVICE COMPANY OF NORTH CAROLINA, INC.

A. PSNC is a corporation organized and existing under the laws of the State of South Carolina, having its principal office and place of business in Gastonia, North Carolina. PSNC is a wholly-owned subsidiary of SCANA, a South Carolina holding company. PSNC is a public utility under the laws of North Carolina and its operations in

[2] Page D-6 of Proxy Statement dated June 15, 2018. Online at https://www.sec.gov/Archives/edgar/data/754737/000119312518193204/d454173ddefm14a.htm.

[3] *Id.* at Page 124, Note 4(g).

this State are subject to the jurisdiction of the Commission pursuant to N.C. GEN. STAT § 62-2. PSNC is primarily engaged in the purchase, sale, transportation, and distribution of natural gas to more than 563,000 customers in North Carolina, within a service territory consisting of all or parts of twenty-eight counties in central and western North Carolina.

Q. PLEASE DESCRIBE DOMINION ENERGY NORTH CAROLINA.

A. Virginia Electric and Power Company, a wholly-owned subsidiary of Dominion Energy, is a public utility operating in the State of North Carolina as DENC. DENC is engaged in the business of generating, transmitting, distributing and selling electric power and energy to the public for compensation, and, as such, its operations in the State are subject to the jurisdiction of the Commission. DENC is also a public utility under the Federal Power Act, and certain of its operations are subject to the jurisdiction of the Federal Energy Regulatory Commission (FERC). DENC is also a member of the regional transmission organization, PJM Interconnection LLC (PJM). DENC serves approximately 120,000 customers in North Carolina, with a service territory of about 2,600 square miles in northeastern North Carolina.

Q. HOW WILL THE MERGER AFFECT THE OWNERSHIP OF PSNC?

A. Under the Merger Agreement, SCANA will become a direct, wholly-owned subsidiary of Dominion Energy and PSNC will remain a direct, wholly-owned subsidiary of SCANA that will continue to exist as a separate legal entity.

Q. PLEASE EXPLAIN THE PURPOSE OF THE REGULATORY CONDITIONS RECOMMENDED BY THE PUBLIC STAFF.

A. As a result of its investigation, the Public Staff developed its recommended Regulatory Conditions, which the Public Staff believes are necessary to ensure that the Merger meets the Commission's three-part test for determining whether a proposed utility merger is justified by the public convenience and necessity, serves the public interest, and affords benefits and protections for North Carolina ratepayers.

Q. PLEASE EXPLAIN THE BENEFITS AND PROTECTIONS OF THE PROPOSED MERGER FOR NORTH CAROLINA RATEPAYERS.

A. Presented below is a description of the Merger benefits and protections proposed in this docket:

Merger-Related Direct Expenses. The Merger–Related Direct Expenses are composed of change-in-control payments made to terminated executives, regulatory process costs, and transaction costs, such as investment banking, legal, accounting, securities issuances and advisory fees. Integration costs include the integration of financial, IT, human resources, billing, accounting, and telecommunications systems. Other transition costs could include severance payments to employees, changes to signage, the cost of transitioning employees to post-merger employee benefit plans, and costs to terminate any duplicative leases, contracts and operations, etc. The Applicants stated that the Merger will not have a net adverse impact on the rates and services of DENC or PSNC. The Applicants further stated that they have not yet determined the transaction fees, integration costs, and any acquisition premium that will result from the Merger, but have committed that none of these costs will be passed on to the customers of PSNC or DENC.

Based on the Public Staff's review of SCANA's Proxy Statement dated June 15, 2018, SCANA has estimated transaction costs of 59.0 million.[4] According to the Companies the incremental change in control payments to SCANA executives could total as much as [BEGIN CONFIDENTIAL] [redacted] [END CONFIDENTIAL].[5] We are recommending that DENC and PSNC file a summary report of their final accounting for Merger-Related Direct Expenses, as well as the calculation of the acquisition premium, within 60 days after the close of the Merger, and supplemental reports, as necessary, within 60 days after each quarter.

Merger-Related Cost Savings. The Applicants stated that the Merger provides only benefits, and no detriment, to the State of North

[4] *Id.* at Page 123, Note 4(b).
[5] Confidential Response to Public Staff Data Request 6-13.

Carolina and to PSNC customers. The Applicants also stated that the economic benefits to customers are currently unquantifiable. The Public Staff is concerned that neither Dominion nor SCANA has quantified benefits to PSNC or DENC ratepayers as has been the case in prior natural gas and electric mergers in this State. In response to data requests regarding projected cost savings and benefits to PSNC ratepayers, the Applicants responded that, while they anticipated benefits and cost savings as a result of the Merger, they were unable to quantify the savings at this time. Due to the lack of concrete information, the Public Staff recommends the merger be subject to the following conditions to ensure sufficient benefits to offset potential costs and risks to PSNC's and DENC's ratepayers: (1) a bill credit to PSNC customers totaling $3.75 million over 3 years; (2) a Rate Moratorium until November 1, 2021 for PSNC's customers; (3) holding DENC and PSNC customers harmless from the impacts of debt downgrades for a period of five years; (4) requiring PSNC to maintain current levels of customer service and behavior towards customers and professional cooperation with regulators, consumer advocates, and intervenors; (5) post-merger opportunities for the electric utility operations of DENC and SCE&G; and (6) other benefits to customers such as the Most Favored Nations Clause that is intended to ensure that North Carolina retail customers receive the benefit of a "Most Favored Nation" status with regard to the provision of Merger benefits and protections among the states involved in this proceeding.

Financing – Ring Fencing and Cost of Debt. The Applicants stated that Dominion Energy, through SCANA, will provide equity, as needed, to PSNC with the intent of maintaining PSNC's current capital structure and credit ratings, and commit to maintain credit metrics that are supportive of strong investment-grade credit ratings for PSNC.

The Public Staff further recommends that additional language be added to the Regulatory Conditions related to the ring fencing and the replacement cost of debt, primarily due to the legal and regulatory uncertainty in South Carolina concerning whether SCE&G is entitled to recovery of costs incurred on its abandoned V.C. Summer nuclear plant and the related recent debt downgrades.

MERGER-RELATED COST SAVINGS

Q. PLEASE EXPLAIN THE PUBLIC STAFF'S RECOMMENDATIONS TO ENSURE POTENTIAL BENEFITS AND COST SAVINGS FOR PSNC AND DENC CUSTOMERS SHOULD THE MERGER BE APPROVED?

A. As stated earlier, the Public Staff is concerned that neither DENC nor SCANA has provided evidence of quantifiable benefits to PSNC or DENC ratepayers. Based on prior mergers approved by this

Commission, the Public Staff believes that some level of cost savings will be realized through integration of the companies in the event the merger is approved and consummated. The Public Staff recommends that PSNC provide a total bill credit of $3.75 million that will be credited to customers in increments of $1.25 million on January 1, 2019, $1.25 million on January 1, 2020, and $1.25 million on January 1, 2021. Based on the proportionate share of expected savings when compared to credits given to customers in past merger proceedings, the Public Staff believes a total payout of $3.75 million is an appropriate amount to flow through to PSNC customers at this time to ensure they receive a quantifiable benefit from cost savings.

Q. HAS THIS COMMMISSION HISTORICALLY APPROVED MERGER SAVINGS IN SUPPORT OF NATURAL GAS COMPANY MERGERS IN THIS STATE?

A. Yes. There have been three mergers involving North Carolina Local Distribution Companies (LDCs) since 1999, and all three have resulted in either rate reductions or one time bill credit for the acquired LDC. In Docket No. G-5, Sub 400, PSNC was acquired by SCANA, and PSNC was required to reduce rates by $1,043,542 within six months of the closing date of its proposed business combination with SCANA and by an additional $1,043,542 within eighteen months of that closing date. In a business combination transaction with Duke Energy Corporation and Piedmont Natural

Gas Company, Inc., (Piedmont) in Docket Nos. E-2, Sub 1095, E-7, Sub 100, and G-9, Sub 682, Piedmont agreed to credit $10 million to its North Carolina customers through a one-time bill credit to be completed by December 31, 2016. The most recent natural gas merger involving an application by Frontier Natural Gas Company (Frontier) and FR Bison Holdings, Inc., and First Reserve Corporation in Docket No. G-40, Sub 136, to acquire one hundred percent (100%) of the stock of Gas Natural, Inc. Frontier agreed to credit $100,000 to its North Carolina customers through a one-time bill credit to be completed by the last day of the first full month following the closing of the merger. (Note that Frontier has 3,800 customers as compared to PSNC's 563,000 and Piedmont's 750,000 North Carolina natural gas customers.)

Q. PLEASE EXPLAIN THE PUBLIC STAFF'S RECOMMENDATION FOR A RATE MORATORIUM FOR PSNC.

A. The Applicants have stated in response to data requests that the savings associated with the merger integration plans may not be fully implemented until December 31, 2019. Therefore, the Public Staff recommends that PSNC not be permitted to increase its non-gas cost margin in its rates before November 1, 2021, except for the following reasons: (1) gas cost adjustments or changes in increments or decrements pursuant to N.C. GEN. STAT. § 62-133.4 and 133.7; (2) to reflect the financial impact of governmental action (legislative, executive or regulatory) having a substantial specific impact on the gas industry generally or on a segment thereof that includes PSNC, including but not limited to major expenditures for environmental compliance; (3) to implement natural gas expansion surcharges imposed pursuant to N.C. GEN. STAT. § 62-158; or (4) to reflect the financial impact of major expenditures associated with force majeure.

For purposes of this condition, the term force majeure means an occurrence that is beyond the control of DENC or PSNC and not attributable to either's fault or negligence. Without limiting the foregoing, force majeure includes acts of nature, like earthquakes, cyclones, rain, tornadoes, hurricanes, flood, fire, acts of the public enemy, war, riots, strikes, mobilization, labor disputes, civil disorders, injunctions-intervention-acts, or failures or refusals to act by government authority; and other similar occurrences beyond the control of the party declaring force majeure which such party is unable to prevent by exercising reasonable diligence. To qualify as an exception, a force majeure event must be reported within 15 working days of its occurrence. Any request pursuant to these exceptions will include a specification of the reasons for the request and an accurate quantification of the financial impact of the request. For purposes of this condition, the "margin rate" is defined as the tariffed sales rate less the benchmark commodity cost of gas, fixed gas cost rate, and temporary increments and/or decrements imposed pursuant to N.C. GEN.STAT. § 62-133.4 and 133.7.

In addition, the Public Staff recommends that PSNC not be allowed to file for new cost deferrals during the rate moratorium time period in order to further protect ratepayers. This condition is designed to protect PSNC's ratepayers from increases in margin rates because of the merger and to ensure that PSNC's ratepayers obtain tangible benefits from the merger. Exceptions are provided for normal gas cost adjustments, governmental actions and significant unexpected events over which PSNC has no control.

Q. HAS THIS COMMMISSION HISTORICALLY APPROVED RATE MORATORIUMS IN SUPPORT OF NATURAL GAS COMPANY MERGERS IN THIS STATE?

A. Yes. In two of the three natural gas merger cases listed above involving North Carolina LDCs, a rate moratorium was approved ranging from two to five years. Since PSNC's last General Rate Case, in Docket No. G-5, Sub 565, was approved by the Commission on October 28, 2016 (PSNC Sub 565 Rate Order), the Public Staff recommends a rate moratorium of approximately three years from the date of the expected order in this docket.

Q. HOW WILL THE RATE MORATORIUM AFFECT PSNC'S INTEGRITY MANAGEMENT TRACKER (IMT)?

A. In the PSNC Sub 565 Rate Order, the Commission found that the proposed IMT expressly provides for Commission review of the mechanism at the earlier of PSNC's next general rate case proceeding or four years from the implementation of the mechanism. Therefore, the Public Staff believes that the IMT can still continue with without PSNC having to file a general rate case.

Q. HAS THE PUBLIC STAFF IDENTIFIED ANY DIRECT BENEFITS OF THE MERGER THAT WILL ACCRUE TO DENC RETAIL ELECTRIC CUSTOMERS?

A. No. In response to a Public Staff data request, Dominion Energy stated that the electric utility operations of Virginia Electric and Power Company (d/b/a DENC) and South Carolina Electric & Gas Company (SCE&G) will remain separate, and the corporate functions will continue to be provided by separate service companies for the foreseeable future. In addition, Dominion stated that there has been no evaluation of joint operational planning, purchasing, and services between the electric utilities, or any affiliate or subsidiary, post-merger. Such joint planning, purchasing, and services is understood to include: (1) Generating Plants – major equipment purchases, leases, spares or reserves, fuel, and maintenance and repair services; (2) Transmission – major equipment purchases, spares or reserves, and maintenance and repair services; and (3) Distribution

– major equipment purchases, spares or reserves, and maintenance and repair services.

Q. DO YOU HAVE ANY RECOMMENDATIONS IN THIS REGARD?

A. Yes. We recommend that the electric utility operations of DENC and SCE&G, along with their affiliates and subsidiaries, look for post-merger opportunities to engage in joint planning, purchasing, and services that will result in cost savings to DENC's retail electric customers, while not compromising reliability or service quality.

FINANCING – RING FENCING & COST OF DEBT

Q. DOES THE PUBLIC STAFF RECOMMEND ADDITIONAL RING FENCING CONDITIONS?

A. Yes. The Public Staff believes there should be additional provisions regarding the replacement cost rate for debt.

Q. DO ANY CREDIT RATING AGENCIES HAVE CONCERNS WITH DOMINION ENERGY'S MERGER WITH SCANA?

A. Yes. As part of the Merger, Dominion Energy would also acquire SCANA's other wholly-owned subsidiary, SCE&G, which is currently embroiled in legal and regulatory actions in South Carolina related to whether it is entitled to recovery of costs incurred on its abandoned V.C. Summer nuclear plant. Following the announcement in July 2017 by SCE&G and Santee Cooper to cease all construction and abandon the nuclear facility, the credit ratings of SCANA, SCE&G, and PSNC declined, as shown in Confidential Public Staff Exhibit 2.

The political uncertainty associated with SCE&G's rate recovery issues and concerns over the decreased cash flow of SCANA have been noted by Moody's Investors Service (Moody's) and S&P. Their concerns were heightened after a federal court's denial of SCE&G's request for a preliminary injunction to halt a 15% rate reduction associated with SCE&G's past recovery of costs incurred on the abandoned nuclear plant. The South Carolina Legislature enacted House Bill 4375, which directed the South Carolina Public Service Commission (SCPSC) to temporarily reduce SCE&G's rates by approximately $31 million per month.[6] On July 2, 2018, the SCPSC implemented the new law, which required SCE&G to implement a rate reduction until a final decision regarding permanent rates for the abandoned nuclear project was determined.[7] Credit rating agencies viewed any incremental and ongoing losses of SCANA as a credit negative to Dominion's acquisition, which is shown in Confidential Public Staff Exhibit 3 and 4.

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[6] 2018 S.C. Acts 258, online at: https://www.scstatehouse.gov/sess122_2017-2018/bills/4375.htm.

[7] SCPSC Docket No. 2018-217-E - Procedure Addressing Implementation of South Carolina General Assembly House Bill 4375, Including Provision of an Experimental Rate as Referenced in S. C. Code Ann. Section 58-34-20. Online at: https://dms.psc.sc.gov/Attachments/Order/0db17176-a490-4527-ac1e-84e35952eb31.

Q. HOW WILL THE MERGER AFFECT THE BORROWING COST FOR PSNC?

A. Given the recent credit downgrades of PSNC and the higher credit ratings of Dominion Energy, it is reasonable to expect that PSNC will be able to obtain long-term debt capital at lower rates than currently are available if a merger with Dominion is consummated. For example, PSNC's June 15, 2018, $100 million issuance of 10-year senior notes was at a 4.33% debt rate; whereas, [BEGIN CONFIDENTIAL] [redacted] [END CONFIDENTIAL] Shown below are the long-term issuer credit ratings by Moody's, and S&P for SCANA Corp., South Carolina Electric & Gas, PSNC, Dominion Energy, and four Dominion Energy subsidiaries.

[8] Applicant's Confidential Response to Public Staff Data Request No. 12-2.

[BEGIN CONFIDENTIAL]

[redacted]	[redacted]	[redacted]
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[redacted]	[redacted]	[redacted]

[redacted]

[END CONFIDENTIAL]

Q. HOW WILL THE MERGER AFFECT THE BORROWING COST FOR DENC?

A. It is not known at this time. The political uncertainty with regard to SCE&G's cost recovery of its abandoned nuclear project in South Carolina may have negative effects on Dominion Energy's financial condition, which could increase the borrowing costs of DENC. As noted in Confidential Public Staff Exhibit 3, [BEGIN CONFIDENTIAL] [redacted]

[redacted] [END CONFIDENTIAL]

Q. DOES THE PUBLIC STAFF BELIEVE THAT THE MERGER WILL MAKE PSNC A FINANCIALLY STRONGER COMPANY?

A. Yes. We believe that the increased financial strength of Dominion Energy, the expectation of PSNC's enhanced credit ratings, and PSNC's greater access to capital markets will make PSNC a stronger company. However, this was the same expectation in the 1999 merger case between SCANA and PSNC.[9] In the 1999 merger proceeding, Charles E. Zeigler, the CEO of PSNC, Mr. William B. Timmerman, the CEO of SCANA, and Public Staff witness Thomas Farmer testified that SCANA's significantly larger size and its progressive and successful management team would facilitate future financial stability.[10] Witness Farmer testified that the merged company would be much larger than PSNC on a stand-alone basis, which should provide an opportunity for PSNC to reduce its capital costs. He noted that the higher debt rating of SCANA and its access to capital would be improved. He concluded by stating that the net result should be a reduction in PSNC's cost of borrowing.[11] As such,

[9] Docket No. G-5, Sub 400: Amended Testimony of Charles E. Zeigler August 19, 1999, page 7 of 9, lines 6-8; Amended Testimony of William B. Timmerman, August 19, 1999, page 9 of 13; Joint Testimony of Public Staff, September 13, 1999, page 6 of 28.
[10] *Id.*
[11] Docket No. G-5, Sub 400, Transcript of Testimony Vol. 7, pp 100-02, 111, heard September 28, 1999.

there are no regulatory conditions that completely insulate utilities from future credit downgrades.

Q. PLEASE EXPLAIN REGULATORY CONDITION 8.2 ON THE REPLACEMENT COST OF DEBT FOR PSNC AND DENC.

A. The Public Staff recommends that the Commission approve this regulatory condition in order to protect PSNC's and DENC's ratepayers from the added risk of a credit downgrade that will lead to higher costs of borrowing than what is appropriate for a LDC comparable to PSNC and an electrical utility comparable to DENC. To accomplish this, the Public Staff recommends that, in the event of a future PSNC debt downgrade that occurs after the Merger and is attributable to the electric utility operations of Dominion Energy, a replacement cost rate for long-term debt for any new financings of PSNC should be employed. The replacement cost rate should assume that PSNC has a credit rating of a "BBB+" by S&P and an "A2" by Moody's for its long-term debt. Similarly, if Dominion Energy has a downgrade that is attributed to the Merger caused, in part, from inadequate cost recovery for SCE&G's Summer units and the political uncertainty in South Carolina; then, a similar replacement cost rate of debt is appropriate for DENC that is based on a "BBB+" by S&P and an "A2" by Moody's for its long-term debt. The Public Staff further recommends that this condition remain in effect for the next five years.

Q. WHY DO YOU RECOMMEND THE USE OF A REPLACEMENT COST RATE OF DEBT BASED ON A "BBB+" LONG-TERM DEBT RATING BY S&P FOR PSNC AND DENC?

A. The Public Staff has selected these ratings by S&P because it is reasonable to expect that PSNC, as a stand-alone company, would have these ratings absent the 2017 and 2018 downgrades associated with SCE&G's abandoned nuclear project. Secondly, these are the current debt ratings of Virginia Electric Power Company and several of its subsidiary companies as noted on Company witness Chapman's Exhibit JRC 2. Third, as shown in Confidential Public Staff Exhibit 2 [BEGIN CONFIDENTIAL] [redacted] [END CONFIDENTIAL]

SERVICE QUALITY

Q. WHAT MERGER COMMITMENTS HAVE BEEN MADE BY DENC AND PSNC RELATED TO SERVICE QUALITY?

A. DENC and PSNC should maintain current levels of customer service and behavior towards customers and professional cooperation with regulators, consumer advocates, and intervenors, Section XI of the proposed Regulatory Conditions address commitments by both DENC and PSNC to provide superior public utility service.

PJM REGULATORY OBLIGATIONS OF DENC

Q. WHAT ARE THE EFFECTS OF THE MERGER ON THE PJM REGULATORY CONDITIONS IMPOSED BY THE COMMISSION ON DENC IN DOCKET NO. E-22, SUB 532?

A. The Public Staff believes that based on the revised regulatory conditions contained in Section VI, as filed in this proceeding, all of the PJM conditions imposed by the Commission in Docket No. E-22, Sub 532 will remain in effect.

MARKET POWER

Q. DOES THE PUBLIC STAFF HAVE ANY MARKET POWER CONCERNS WITH THE MERGER?

A. Our review of the Company witness Hunger's testimony, Dominion Energy and SCANA Corp. (Applicants) joint application under Section 203 of the Federal Power Act, and the July 12, 2018, FERC Order[12] support the findings that the Merger is in the public interest. The FERC Order notes that the retail rates of Dominion Virginia and DENC's, and SCE&G will be regulated by the Virginia, North Carolina, and South Carolina regulatory commissions, respectively and that there is no geographic overlap of service areas.[13] With respect to market power with the wholesale gas sector, the

[12] *Dominion Energy, Inc.*, 164 FERC ¶ 62,025 (July 12, 2018), online at: https://elibrary.ferc.gov/idmws/common/opennat.asp?fileID=14970923.
[13] *Id.*

Applicants noted that the combined share of firm capacity is about 21 percent (taking into account the completion of the Atlantic Coast Pipeline, Transco Sunrise pipeline, and the Mountain Valley Pipeline in 2018 and 2019) and that pipeline customers do not have the ability to withhold capacity or take actions that would raise costs to rivals. Furthermore, the Public staff's recommended Regulatory Conditions and Code of Conduct provide cost allocation and pricing standards, natural gas marketing standards, requirements regarding the sharing of potentially competitively sensitive information, and requirements to file cost allocation manuals and annual reports on affiliate transactions which should work to minimize any market power of the merged company. Public Staff Exhibit 5 presents the total MW generation segmented by fuel and by the ultimate owners for Duke Energy Corporation, Dominion Energy, Inc., SCANA Corporation and the MW generated by other owners in the three states of Virginia, North Carolina, and South Carolina, showing that the combined companies still rank behind Duke Energy in total MW generation.

<u>OTHER RECOMMENDATIONS</u>

Q. PLEASE DESCRIBE THE PUBLIC STAFF'S RECOMMENDATION THAT THE MERGER CONTAIN A MOST FAVORED NATION CLAUSE.

A. A most favored nation clause ensures that PSNC and DENC customers in North Carolina will be treated no worse than customers in other jurisdictions as a result of the merger.

Following the approval of the Merger by the state commissions of Georgia, South Carolina, and any other jurisdictions where DENC or PSNC must obtain approval, and approval of merger-related affiliate agreements and any other merger-related filings required to be or otherwise approved by any applicable jurisdiction, any mechanisms pursuant to which benefits and ratepayer protections are provided to DENC and/or PSNC retail customers in each of these states should be reviewed to identify the states in which each utility's retail customers will receive the largest financial (including, but not limited to, rate reductions, rebates, refunds, other payments, bill credits, rate moratoriums, etc.) and non-financial benefits, and other ratepayer protections, on a per customer or pro rata basis. If the application of those benefits to either utility's North Carolina retail ratepayers would result in a greater level of benefits and/or protections than that which has otherwise been provided for North Carolina retail customers in these Regulatory Conditions, then the benefits and protections to that utility's North Carolina retail ratepayers should be increased to match the greatest level of benefits and protections provided to the retail ratepayers in any of the other jurisdictions.

Application of this methodology is intended to ensure that North Carolina retail customers receive the benefit of a "Most Favored Nation" status with regard to the provision of Merger benefits and protections among the states named above. In no event will the application of the methodology because North Carolina retail customers' benefits or protections to be reduced. To facilitate this review, DENC and PSNC should jointly to file final Orders, Stipulations, etc. from all jurisdictions listed above.

Q. WHAT IS THE PUBLIC STAFF'S RECOMMENDATION WITH REGARD TO THE PROPOSED MERGER?

A. The Public Staff recommends that the proposed Merger of Dominion and SCANA be approved, subject to the conditions outlined above and the provisions of its proposed Regulatory Conditions and the Code of Conduct, which varies from those filed by the Applicants. The Public Staff, however, intends to engage in settlement negotiations with the Applicants to attempt to reach agreement on the Regulatory Conditions and Code of Conduct.

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

A. Yes.

APPENDIX A

QUALIFICATIONS AND EXPERIENCE

MICHAEL C. MANESS

I am a graduate of the University of North Carolina at Chapel Hill with a Bachelor of Science degree in Business Administration with Accounting. I am a Certified Public Accountant and a member of both the North Carolina Association of Certified Public Accountants and the American Institute of Certified Public Accountants.

As Director of the Accounting Division of the Public Staff, I am responsible for the performance, supervision, and management of the following activities: (1) the examination and analysis of testimony, exhibits, books and records, and other data presented by utilities and other parties under the jurisdiction of the Commission or involved in Commission proceedings; and (2) the preparation and presentation to the Commission of testimony, exhibits, and other documents in those proceedings. I have been employed by the Public Staff since July 12, 1982.

Since joining the Public Staff, I have filed testimony or affidavits in several general, fuel, and demand-side management/energy efficiency rate cases of the utilities currently organized as Duke Energy Carolinas, LLC, Duke Energy Progress, LLC, and Virginia Electric and Power Company (Dominion Energy North Carolina) as well as in several water and sewer general rate cases. I have also filed testimony or affidavits in other proceedings, including applications for certificates of public convenience and necessity for the construction of generating facilities, applications for approval of self-generation deferral rates, applications for approval of cost and incentive recovery mechanisms for electric utility demand-side management and energy efficiency (DSM/EE) efforts, and applications for approval of cost and incentive recovery pursuant to those mechanisms.

I have also been involved in several other matters that have come before this Commission, including the investigation undertaken by the Public Staff into the operations of the Brunswick Nuclear Plant as part of the 1993 Carolina Power & Light Company fuel rate case (Docket No. E-2, Sub 644), the Public Staff's investigation of Duke Power's relationship with its affiliates (Docket No. E-7, Sub 557), and several applications for business combinations involving electric utilities regulated by this Commission. Additionally, I was responsible for performing an examination of Carolina Power & Light Company's accounting for the cost of Harris Unit 1 in conjunction with the prudence audit performed by the Public Staff and its consultants in 1986 and 1987.

I have had supervisory or management responsibility over the Electric Section of the Accounting Division since 1986, and also was assigned management duties over the Water Section of the Accounting Division during the 2009-2012 time frame. I was promoted to Director of the Accounting Division in late December 2016.

APPENDIX B

QUALIFICATIONS AND EXPERIENCE

JAN A. LARSEN

I graduated from North Carolina State University in 1983 with a Bachelor of Science degree in Civil Engineering. I was employed with Law Engineering Testing Company as a Materials Engineer from 1983 to 1984. From 1984 until 1986, I was employed by the North Carolina Department of Transportation as a Highway Engineer.

In 1986, I was employed by the Public Staff's Water Division as a Utilities Engineer I. In 1992, I was promoted to Utilities Engineer II with the Public Staff's Natural Gas Division and promoted to Utilities Engineer III in 2002.

In May of 2016, I was promoted to the Director of the Public Staff's Natural Gas Division. My most current work experience with the Public Staff includes the following topics:

1. Rate Design
2. Allocated Cost-of-Service Studies
3. Purchase Gas Cost Adjustment Procedures
4. Tariff Filings
5. Natural Gas Expansion Project Filings
6. Depreciation Rate Studies
7. Annual Review of Gas Costs
8. Weather Normalization Adjustments
9. Customer Utilization Trackers / Margin Decoupling Trackers
10. Feasibility Studies / Line Extension Policies
11. Pipeline Integrity Management Riders
12. Mergers and Acquisitions

APPENDIX C

QUALIFICATIONS AND EXPERIENCE

JOHN ROBERT HINTON

I received a Bachelor of Science degree in Economics from the University of North Carolina at Wilmington in 1980 and a Master of Economics degree from North Carolina State University in 1983. I joined the Public Staff in May of 1985. I filed testimony on the long-range electrical forecast in Docket No. E-100, Sub 50. In 1986, 1989, and 1992, I developed the long-range forecasts of peak demand for electricity in North Carolina. I filed testimony on electricity weather normalization in Docket Nos. E-7, Sub 620, E-2, Sub 833, and E-7, Sub 989. I filed testimony on customer growth and the level of funding for nuclear decommissioning costs in Docket No. E-2, Sub 1023. I filed testimony on the level of funding for nuclear decommissioning costs in Docket Nos. E-7, Sub 1026 and E-7, Sub 1146. I have filed testimony on the Integrated Resource Plans (IRPs) filed in Docket No. E-100, Subs 114 and 125, and I have reviewed numerous peak demand and energy sales forecasts and the resource expansion plans filed in electric utilities' annual IRPs and IRP updates.

I have been the lead analyst for the Public Staff in numerous avoided cost proceedings, filing testimony in Docket No. E-100, Subs 106, 136, 140, and 148. I have filed a Statement of Position in the arbitration case involving EPCOR and Progress Energy Carolinas in Docket No. E-2, Sub 966. I have filed testimony in applications of avoided cost for cost recovery of energy efficiency programs and demand side management programs in Dockets Nos. E-7, Sub 1032, E-7, Sub 1130, E-2, Sub 1145, and E-2, Sub 1174.

I have filed testimony on the issuance of certificates of public convenience and necessity (CPCN) in Docket Nos. E-2, Sub 669, SP-132, Sub 0, E-7, Sub 790, E-7, Sub 791, and E-7, Sub 1134.

I have filed testimony on the issue of fair rate of return in Docket Nos. E-22, Sub 333; E-22, Sub 412; P-26, Sub 93; P-12, Sub 89; G-21, Sub 293;P-31, Sub 125; G-5, Sub 327; G-5, Sub 386; G-9, Sub 351; P-100, Sub 133b; P-100, Sub 133d (1997 and 2002); G-21, Sub 442; W-778, Sub 31; and W-218, Sub 319, E-22, Sub 532, and W-218, Sub 497 and in several smaller water utility rate cases.. I have filed testimony on credit metrics and the risk of a downgrade in Docket No. E-7, Sub 1146.

I have filed testimony on the hedging of natural gas prices in Docket No. E-2, Subs 1001 and 1018. I have filed testimony on the expansion of natural gas in Docket No. G-5, Subs 337 and 372. I performed the financial analysis in the two audit reports on Mid-South Water Systems, Inc., Docket No. W-100, Sub 21. I testified in the application to transfer of the CPCN from North Topsail Water and Sewer, Inc. to Utilities, Inc., in Docket No. W-1000, Sub 5. I have filed testimony on rainfall normalization with respect of water sales in Docket No. W-274, Sub 160.

With regard to the 1996 Safe Drinking Water Act, I was a member of the Small Systems Working Group that reported to the National Drinking Water Advisory Council of the U.S. Environmental Protection Agency. I have published an article in the National Regulatory Research Institute's Quarterly Bulletin entitled Evaluating Water Utility Financial Capacity.

APPENDIX D

QUALIFICATIONS AND EXPERIENCE

JAMES S. MCLAWHORN

I graduated with honors from North Carolina State University with the Bachelor of Science Degree in Industrial Engineering in May of 1984. I received the Master of Science Degree in Management with a finance concentration from North Carolina State University in December of 1991. While an undergraduate, I was selected for membership in both Tau Beta Pi and Alpha Pi Mu engineering honor societies.

I began my employment with the Public Staff Communications Division in June of 1984. While with the Communications Division, I testified before the Commission in general rate proceedings regarding matters of telephone quality of service.

In September of 1987, I was employed by GTE-South as an engineer in the Capital Recovery Department. I was responsible for analysis and Recommendations to Company management regarding appropriate depreciation rates for recovery of the Company's capital investments.

I began my employment with the Electric Division of the Public Staff in November of 1988. I assumed my present position as Director of the Electric Division in October of 2006. It is my responsibility to supervise, and make policy recommendations on, all electric utility matters pending before the Commission.

I have testified previously before the Commission in numerous proceedings including Duke Energy Carolinas, LLC's Rate Cases, Docket No. E-7, Subs 487, 909, 989, and 1146; Duke Energy Progress, LLC's Rate Cases, Docket No. E-2, Subs 1023 and 1142; Virginia Electric and Power Company's Rate Cases, Docket No. E-22, Subs 314, 333, 412, and 532; New River Light and Power Company Rate Cases, Docket No. E-34, Subs 28 and 32; Nantahala Power and Light Company Rate Case Docket No. E-13, Sub 157; in the Application of Dominion North Carolina Power to join PJM in Docket No. E-22, Sub 418; in Duke Power Company's request to merge with Cinergy Corporation in Docket No. E-7, Sub 795; in Duke Energy Carolinas, LLC's request for approval of its Save-A-Watt cost recovery model in Docket No. E-7, Sub 831; and, in the Generic Investigation into Section 111 of the 1992 Energy Policy Act in Docket No. E-100, Sub 69.