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Issue: Commissioner Questions - Financings
Witness: Robert B. Hevert
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Sponsoring Party: The Empire District Electric Company
Case No.: ER-2019-0374
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Before the Public Service Commission
of the State of Missouri

Supplemental Testimony to Address Commissioner Questions

of

Robert B. Hevert

on behalf of

The Empire District Electric Company
a Liberty Utilities Company

May 6, 2020

Liberty Utilities
EMPIRE DISTRICT

SUPPLEMENTAL TESTIMONY TO ADDRESS COMMISSIONER QUESTIONS
OF
ROBERT B. HEVERT
THE EMPIRE DISTRICT ELECTRIC COMPANY
BEFORE THE
MISSOURI PUBLIC SERVICE COMMISSION
CASE NO. ER-2019-0374

I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Robert B. Hevert and my business address is ScottMadden, Inc., 1900 West Park Drive, Suite 250, Westborough, MA, 01581.

Q. Are you the same Robert B. Hevert who submitted direct, rebuttal, and surrebuttal testimony in this matter on behalf of The Empire District Electric Company ("Empire")?

A. Yes.

Q. What is the purpose of your supplemental testimony in this proceeding?

A. My Supplemental Testimony addresses a specific question directed to Empire by the Missouri Public Service Commission ("Commission"). In particular, I address question five regarding Issue 18 - Affiliate Transactions, contained in the "Commission Questions" issued April 28, 2020.

II. RESPONSE

Q. Please briefly summarize affiliate transactions question five as it relates to your surrebuttal testimony.

A. Question five refers to page 62 of my Rebuttal Testimony, where I discussed Office of the Public Counsel ("OPC") witness Mr. Murray's position that Liberty Utilities

Co. ("LUCo") issued $395 million of long-term debt to fund equity investments in its regulated utilities. My Rebuttal Testimony explained that such "double leverage" arguments fail to consider that it is the risk of the investment, not the source of funds that determines how operating utilities are capitalized, and the costs of that capital. In that context, my Rebuttal Testimony further explained "it is the utility's operating risk that defines the capital structure and cost of capital, not investors' sources of funds."[1]

Question five notes it could be inferred from that statement that Empire's $90 million financing from LUCo was priced not only based on historical long-term debt, but also on Empire's operating risk. The question then points to Mr. Timpe's Rebuttal Testimony, where he stated that the terms of Empire financing was "based on the weighted average life of LUCo's March 2017 financing and was equivalent to the term of Liberty-Empire's last pre-acquisition financing in August 2015, thereby making the term consistent with past practice at 'old Empire.'"[2] Question five then asks the Company to explain if factors beyond those mentioned by Mr. Timpe were considered in determining the pricing for Empire's financing.

Q. Please now provide your response to question five.

A. Question five refers to page 8 of Mr. Timpe's Rebuttal Testimony, which speaks to the $90 million financing's tenor, and pricing. Regarding the fifteen-year term, Mr. Timpe explains it was "equivalent to the term of Liberty-Empire's last pre-acquisition financing in August 2015, thereby making the term consistent with past practice at 'old Empire'".[3] As to pricing, Mr. Timpe notes it was "based on the credit spreads

[1] *See*, Commission Questions, at 11, Rebuttal Testimony of Robert B. Hevert (Ex. 37), at 60 – 62.
[2] Commission Questions, at 11.
[3] Rebuttal Testimony of Mark T. Timpe (Ex. 43), at 8.

LUCo obtained from its highly competitive $750 million unsecured financing in March 2017"[4], which Mr. Timpe states was nearly three times over-subscribed.[5]

Regarding the question of whether the $90 million financing reflects factors beyond those discussed at page 8 of Mr. Timpe's Rebuttal Testimony, there are two points to consider. First, as noted in my Rebuttal Testimony, a common financing principle is "maturity matching" under which the weighted average life (or duration) of the securities in the capital structure is matched with the average life of the assets being financed.[6] My Direct Testimony noted maturity matching addresses financing risk[7], which is a common concern for capital-intensive enterprises such as utilities. In short, the capital-intensive nature of utility operations requires long-lived assets, which require long-term sources of financing.

As Mr. Timpe points out, the $90 million financing's fifteen-year tenor is consistent with the Company's past practice of financing long-lived assets with long-term securities. Because that financing practice arises from and reflects the nature of utility operations, it was a factor appropriately reflected in the $90 million financing's tenor.

Regarding the financing's pricing, Mr. Timpe explains it was based on credit spreads reflecting LUCo's 2017 $750 million financing.[8] Consequently, they too reflect the risks of utility operations. That said, because the 2017 financing was many times larger than the $90 million financing at issue in question five, and knowing the 2017 financing was over-subscribed by a factor of nearly three, the credit spreads

[4] Rebuttal Testimony of Mark T. Timpe (Ex. 43), at 8.
[5] Rebuttal Testimony of Mark T. Timpe (Ex. 43), at 8
[6] Rebuttal Testimony of Robert B. Hevert (Ex. 37), at 58 – 60.
[7] Direct Testimony of Robert B. Hevert (Ex. 36), at 39-40.
[8] Rebuttal Testimony of Mark T. Timpe (Ex. 43), at 8.

likely were narrower than they would have been for a single, contemporaneous $90 million offering. In any case, because it was based on the Company's $750 million financing, the pricing for the $90 million financing reflected the risks associated with utility operations.

To summarize, the $90 million financing's tenor is consistent with the practice of financing long-lived utility assets with long-lived debt, and its pricing was set by reference to an over-subscribed utility financing, also reflecting the risks of utility operations. Both the tenor and the pricing therefore reflected utility risks and operations.

Q. Does this conclude your supplemental testimony?

A. Yes.

VERIFICATION OF ROBERT B. HEVERT

Robert B. Hevert, under penalty of perjury, declares that the foregoing supplemental testimony is true and correct to the best of his knowledge, information, and belief.

/s/*Robert B. Hevert*
Robert B. Hevert